[2017] UKFTT 0320 (TC)

TC05798

Appeal number: TC/2016/01738

CAPITAL GAINS TAX – residence status – whether appellant resident or ordinarily resident in relevant years – whether s 10A TCGA applies – whether appellant trading as property dealer so as to eliminate chargeable gains – whether lost deposit and other payments deductible in property dealing trade or for CGT – whether appellant chargeable as non-resident trading in the UK – whether if chargeable as a trader profits could be assessed – penalties for incorrect returns and failure to file returns – whether correctly imposed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

ELIZABETH MARSH **Appellant**

- and -

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

TRIBUNAL: JUDGE RICHARD THOMAS
MOHAMMED FAROOQ

Sitting in public at Fox Court, London EC1 on 30 March 2017

Mr Richard Baptiste of Baptiste & Co, Chartered Certified Accountants, for the Appellant

Mrs Beverley Levy, Appeals & Reviews, Solicitor's Office of HM Revenue and Customs, for the Respondent

DECISION

1. On the surface this was a fairly straightforward case of assessments for two years to capital gains tax (“CGT”) on chargeable gains on real property which had not been returned and the penalties consequent on the failure to return the gains. But from the facts as they emerged at the hearing there were a number of quite awkward issues potentially to be resolved.

2. First though we had to deal with the non-attendance of the appellant. On 23 March 2017 Mr Baptiste, the appellant’s accountant, wrote to the Tribunal stating that his client works abroad and would not be in the UK on the date of the hearing. He offered a number of dates between June 2017 and January 2018 when she would be in the country and he asked for a hearing falling within the period of presence in the UK.

3. Mrs Levy on behalf of HMRC objected to the adjournment of the case on the grounds that the date of the hearing had been known to the appellant since 27 January 2017 and that she had not given any dates to avoid in response to the Tribunal’s request.

4. On 27 March 2017 the Tribunal informed Mr Baptiste that the judge considering the application had turned down the request for the reasons given by HMRC, but that he would be able to renew his request orally at the hearing.

5. This is indeed what Mr Baptiste did, giving as his reasons those which he had previously given and adding that his client was a development consultant and was currently in a remote area in Sierra Leone where communication was difficult.

6. Under Rule 33 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 where a party is not present we are required to consider whether it is in the interests of justice to proceed.

7. It seemed to us from the papers that Mr Baptiste had been conducting the correspondence with HMRC and was fully appraised of the issues and indeed that as those issues were primarily tax and legal issues, the appellant would be unable to add any more or produce any more evidence than she had already done through Mr Baptiste and by phone calls to HMRC. We also noted that this was not the first application for adjournment.

8. We decided that given the circumstances it was in the interests of justice to proceed.

Facts

9. We set out below the basic facts of the case which we have taken from the documents in the bundle prepared by HMRC and which we find as facts.

10. On 6 April 2007 the appellant was notified that HMRC required her to complete a tax return for the year of assessment 2006-07. A return was received by HMRC on 1 February 2008. It was filed by Baptiste & Co.

11. The return showed no income and no chargeable gains. There was a "white space" entry "During this tax year I [w]as not uk resident".

12. On 6 April 2008 the appellant was notified that HMRC required her to complete a tax return for the year of assessment 2007-08. No such return has ever been received by HMRC.

13. On 14 February 2013 HMRC began a "compliance check" into the appellant's income tax and capital gains tax ("CGT") position. The letter opening the check did not state the periods with which it was concerned but it contained a schedule of information that HMRC wished to see, and since the information covered the period 6 April 2006 to 5 April 2008 we find that the tax years in issue were 2006-07 and 2007-08. The information sought concerned real property owned by the appellant including dates of purchase and sale, use of the property and details of any income received from them.

14. On 20 March 2013 HMRC issued a notice under Schedule 36 FA 2008 for the information.

15. On 5 April 2013 HMRC issued an assessment charging £12,391, being tax charged on income from property of £7,000 and on chargeable gains of £46,200 (this appears to be the amount *after* deducting the annual exempt amount given by s 4 Taxation of Chargeable Gains Act 1992 ("TCGA")). This was said to be a protective assessment based on the information held by HMRC.

16. On 21 August 2013 the appellant contacted HMRC by phone. In the course of the conversation she asked if she was liable to tax in the two years concerned as she had been employed in Boston. HMRC said they needed to look at the facts.

17. On 25 September 2013 the appellant contacted HMRC from South Africa and was told about the reasons for HMRC's enquiries and the assessment. She informed HMRC that she would be returning to the UK and would discuss with HMRC how to proceed. HMRC agreed to "put the case on hold" until her return.

18. On 26 February 2014, following no further contact from the appellant, HMRC wrote to her to say that, unless the information being sought was provided within 30 days, HMRC would issue "closure notices" (*sic*) for 2006-07 and 2007-08 and "tax assessments" for the same years. The letter informed her that there was an inaccuracy in the 2006-07 return being the omission of a gain of £55,000 from a property and of income of £8,565 from rents, both figures based on information held by HMRC.

19. The letter added that for 2007-08 there had been no return but there were two disposals of real property giving rise to gains of £102,000 and £105,000 which had not been returned. A calculation of the CGT due for 2007-08 was attached which showed CGT of £69,937.

20. On 21 March 2014 HMRC wrote to the appellant about penalties which they proposed to charge under s 95 and s 93(5) Taxes Management Act 1970 ("TMA") on the basis of her negligent conduct in making an incorrect return for 2006-07 and not making a return at all for 2007-08. The proposed abatement was 70% (thus the penalty was 30% of the tax omitted or not returned.

21. On 29 March 2014 the appellant called HMRC. During the call HMRC raised the issue of residence and explained s 10A TCGA to the appellant. The appellant was told that as she was non-resident for only two years s 10A would probably apply.

22. Around this time the appellant had authorised Baptiste & Co to receive and conduct correspondence on her behalf (using Form 64-8).

23. In a letter dated 28 March Baptiste & Co provided information about the property transactions and informed HMRC that the appellant was not resident in the UK between 6 June 2004 and 30 June 2006 and between 1 October 2007 and May 2008, adding that this meant she was not resident in the UK for 2004/05, 2005/06 and 2007/08.

24. The information given about two properties showed that one was empty for a few months before sale but was let for nearly three years and the other was empty for four months before sale and seven months overall, but was let for three years.

25. On 3 April 2014 HMRC issued a discovery assessment for the tax year 2007-08. This was said to be issued under s 29(4) TMA (loss of tax brought about carelessly or deliberately) a section which was said to extend the time limit for assessing to six years. The figures used were those shown in §19.

26. On 8 and 22 April 2014 HMRC addressed residence issues with Baptiste & Co. Their view was that the appellant was resident in 2006-07 and 2007-08 as the split years concession D2 did not apply. But even if she was non-resident it was their view that s 10A applied.

27. On 30 April 2014 Baptiste & Co stated their disagreement on residence for income tax for 2006-07 but accepted that the "5 year rule" meant that the appellant was "UK resident for CGT". On 22 August 2014 they clarified their view: the client was non-resident for 2007-08.

28. Throughout 2014 there was correspondence about the calculation of the chargeable gains.

29. On 24 March 2015 Baptiste & Co suggested that:

> "having held detailed discussions with my client about the nature of her activities, it is now clear to me that we need to re-examine the entire basis of her activities.
>
> I now believe that my client was trading in property and a Sch D1 is more appropriate."

30. On 13 April 2015 HMRC responded asking for details and supporting evidence of trading.

31. On 3 August 2015 Baptiste & Co provided a large amount of documentation. This included accounts for the property trading activity for the years 2003-04 to 2007-08 and information to support certain deductions in the accounts.

32. Correspondence continued about the calculation of the gain, and from information they had compared with that supplied HMRC came to the view that the sale price of one property had been understated by £60,000. Correspondence also contained argument back and forth about the "trading v investment" issue.

33. On 20 October 2015 HMRC set out their final view of their compliance check, with calculations of the additional tax due. For 2006-07 no income was shown, and the chargeable gains were £23,633 after the annual exempt amount ("AEA") was deducted. For 2007-08 no income was shown and the and the chargeable gains were £116,968 after the AEA.

34. Information from the appellant relayed to HMRC by Baptiste & Co on 10 November 2015 referred to "the failed purchase of 80 Weymouth Terrace". She also said that she had a "property trading business account" with Lloyds TSB which she used to purchase the property.

35. On 16 November 2015 the appellant called HMRC and questioned whether she owed tax due to her non resident status. HMRC explained s 10A TCGA again.

36. On 7 December 2015 HMRC issued penalty determinations for 2006-07 for £2706.96 and for 2007-08 for £23,786.52.

37. On that date HMRC also issued a "Notice of amended assessment" for 2006-07 showing a reduction of from £12.391 to £4,511.60 and a "Notice of amended assessment" for 2007-08 showing a reduction from £69,937 to £39,644.

38. On 4 January 2016 Baptiste & Co appealed against the assessments raised on 7 December.

39. On 22 March 2016 a Notice of Appeal was sent to the Tribunal.

Legal framework

40. Appendix 1 to the decision sets out the law relating to the territorial scope of CGT, the interaction of income tax and CGT and the provisions relating to deductions including for forfeited deposits.

41. We remark here that we have, fortunately, not relied on the legislation in HMRC's bundle. The version of s 10A TCGA that they cited was that applying currently. This section 10A was substituted for the previous version in FA 2013 as a result of the enactment of the statutory residence test and the abolition of the concept of ordinary residence (at least for tax purposes). The correct version is very different and is the one set out in the Appendix. The Tribunal has on more than one occasion criticised

HMRC for giving the wrong year's legislation. When the years in issue are 10 years before the year of the hearing it is almost inevitable that the law will not be exactly the same then as now. It ought not to happen.

42. Appendix 2 to the decision sets out the law relating to the territorial scope of income tax on trading income, and relevant provisions on the calculation of profits.

43. Appendix 3 to the decision sets out the law relating to discovery assessments, time limits for assessing and the penalties imposed in this case.

Discussion: introductory

44. The issue of discovery and carelessness is a threshold issue. If HMRC fail on this then the remaining "technical issues" are moot. But to decide the question whether there was a discovery of a loss of tax and whether the appellant's conduct was careless does it seems to us in this particular case require us to given detailed consideration to the technical issues. And if we agree that HMRC have made valid discovery assessments we will have in any case to consider those technical issues.

45. We therefore consider first the issues relating to, or determined by the question of residence, the question whether the appellant was trading and if so what the trading profits are and the question whether the computation of the chargeable gains is correct (disregarding the trading question).

46. Then by reference to our findings on these issues, we consider the procedural issues of the discovery assessments and the penalties.

47. But before any of that we must consider what appeals are actually before us, a matter which was also not as straightforward as it might have been.

Discussion: what appeals?

48. Our suspicions that all was not straightforward were aroused when HMRC stated that we had before us appeals against amended assessments. We asked Mrs Levy how it was possible for an assessment which is not a self-assessment to be amended by HMRC otherwise than as a result of a determination by a Tribunal or its deemed equivalent, an agreement under s 54 TMA. She had no answer and agreed with us that the purported amendments were a nullity, as therefore were the purported appeals against them.

49. Mrs Levy agreed then that the assessments in question were the "protective" assessments issued in April 2013 and April 2014. We asked where the appeals against those assessments were to be found but Mrs Levy could not point to them.

50. We continued the hearing in any event, and having looked more closely at the papers and in particular at HMRC's agreement on 25 September 2013 to put matters "on hold" (see §17) we are prepared to treat the appeals against the amended assessments as appeals against the protective assessments with HMRC having by their conduct waived any issue of lateness. The appeals against the penalties were made in time.

Discussion: the residence etc issues

Residence and ordinary residence

51. We asked Mr Baptiste if the residence position was agreed as seemed to be the case from the papers. He said that the residence position needed to be looked into. We were not sure what he wanted us to look into. He had it seems argued that for income tax purposes the appellant was not resident in 2004-05, 2005-06 and 2007-08 and he had said that for CGT purposes the effect of s 10A TCGA was to deem her to be resident (by which we assume he meant that residence made no difference to the outcome).

52. We do not fully understand what his accepting the appellant's residence for income tax purposes signified. It may be that he had in mind that the information about the properties he gave to HMRC showed that there was rental income arising to the appellant in those years. However that would not be relevant to residence as income tax on UK property business income (or Schedule A income in 2004-05) is charged on non-residents as on residents.

53. And it seems also to be assumed by Mr Baptiste that the appellant was non-resident in 2006-07: at least that is what was said in the only entry on the return he filed for her for that year.

54. Curiously HMRC included rental income for 2006-07 in the protective assessment for that year but then removed it in the so called amendment to that assessment. No rental income was charged in the 2007-08 assessment: it maybe that none arose in the period before sale of the relevant properties falling in 2007-08.

55. From the material we have seen we find as a fact that the appellant was outside the United Kingdom from 30 June 2006 to 1 October 2007.

56. We also find that HMRC accepted that she was non-resident in both years (in a note of a telephone conversation with the appellant on 29 March 2014) and relied on s 10A TCGA 1992 to charge the gains on the properties to CGT.

57. The only information as to where the appellant was resident in the gap period was in her telephone call to HMRC on 21 August 2013 when she said she had been living in Boston (Massachusetts, we assume) in the period.

58. On the basis that the burden of proof of residence is on HMRC (regardless of the burden on them to justify the assessments and penalties) and in the light of our findings of fact and her claim in the 2006-07 return to be non-resident, we consider that the appellant was not resident in the United Kingdom in 2006-07 and 2007-08. That the burden of proof is on HMRC can be seen from *Cesena Sulphur Co Ltd v Nicholson (Surveyor of Taxes)* 1 TC 88 cited and approved in *Untelrab Ltd and others v McGregor (HM Inspector of Taxes)* [1996] STC (SCD) 1).

59. CGT is also chargeable on all gains made by a person who, although non-resident, is ordinarily resident. We do not have sufficient information to establish whether the

appellant was ordinarily resident in the year. It is clear from the papers that she was outside the UK for extensive periods before 2006 and that she has also been outside the UK in periods since 2008 and continues to be. As the burden of proof of showing ordinary residence must also be on HMRC, we consider that she was not ordinarily resident in the United Kingdom in those two years.

Section 10A TCGA 1992

60. HMRC rely however, as we have noted, on s 10A TCGA 1992. The first question raised (s 10A(1)(a)) is whether in a year the appellant satisfied the residence requirement which is (s 10A(9)) that in any part of the year the individual is resident or ordinarily resident in the United Kingdom. It appears from the information we have that the appellant was resident in 2008-09, which is called by s 10A "the year of return".

61. The next question (s 10A(1)(b)) is whether there are years of assessment immediately preceding 2008-09 in which the appellant was not resident. There are: 2006-07 and 2007-08 at least.

62. The third question (s 10A(1)(b)) is whether there are years of assessment before 2008-09 in which the appellant was resident. It seems from the papers that there is no suggestion that she was not resident in 2003-04.

63. The fourth question (s 10A(1)(c)) is whether there are fewer than five years of assessment falling between the year of departure and the year of return. "Year of departure" means "the last year of assessment before the year of return for which the taxpayer satisfied the residence requirements" (s 10A(8)) so in this case that year is 2003-04. There are then four years between the year of departure and the year of return, so fewer than five.

64. The fifth question (s 10A(1)(d)) is whether "four out of the seven years of assessment immediately preceding the year of departure" are also years of assessment for each of which the appellant satisfied the residence requirements. There is no suggestion by the appellant that there were not.

65. We hold therefore that in this case s 10A(1) applies to the appellant.

66. Where s 10A(1) applies, TCGA applies as if all the "chargeable gains and losses" which would have accrued to the appellant in the "intervening years" if s 10A is ignored were gains or losses accruing in the year of return (s 10A(2)).

67. The "intervening years" are defined in s 10A(8) to mean:

> "any year of assessment which, in a case where the conditions in paragraphs (a) to (d) of subsection (1) above are satisfied, falls between the year of departure and the year of return".

In this case 2006-07 and 2007-08 are intervening years.

68. The next question is whether the gains accruing to the appellant in 2006-07 and 2007-08 are “chargeable gains”.

69. Since every gain is, unless otherwise provided, a chargeable gain (s 15(2) TCGA) the gains made on real property in 2006-07 and 2007-08 are chargeable gains. There is no suggestion for example that the exemption for principal private residences (s 223 TCGA) applies which would make a gain not a chargeable gain. And even though s 10 TCGA limits the charge to CGT on non-residents to those gains arising from certain assets in the UK of the permanent establishment (“PE”) of a trade, that does not make other gains made by a non-resident not chargeable gains.

70. The result is that the gains made by the appellant in 2006-07 and 2007-08 are gains falling within s 10A TCGA, as HMRC argue.

71. But this conclusion is subject to s 10A(3) which treats certain gains as not accruing to the appellant. Those gains are (by virtue of s 10A(3)(a)) gains on assets acquired by the appellant in the year of departure or any intervening year in which the appellant was not resident and in which the other conditions in s 10A(3)(b) to (d) apply.

72. The assets in this case were acquired in 2003-04 and 2005-06. The first is the year of departure and the second is an intervening year. None of paragraphs (b) to (d) of s 10A(3) apply so therefore the gains do not fall within s 10A(2) and are not gains which can be assessed on the appellant.

73. But in any case even if they did not fall within the exclusion in s 10A(3) they would be treated by s 10A(2) as accruing in the year of return, which is 2008-09. No assessment to CGT has been made for that year of assessment. It follows that the assessments to CGT for 2006-07 and 2007-08 are not competent, unless there is in those years a charge to CGT by virtue of s 10 TCGA.

Section 10 TCGA 1992

74. Whether s 10 is capable of applying depends on whether the appellant had a “branch or agency” in the United Kingdom through which she carried on her alleged trade of property dealing in the two years of assessment concerned.

75. We preface the next passages by saying that we were not addressed orally or in HMRC’s statement of case on either s 10 TCGA or on the question whether, if there was a trade, there was a branch or agency in the UK thorough which it was conducted. What follows is therefore our tentative thinking on the issue in which we assume without deciding that there was a trade with a UK branch or agency.

76. Section 10(1) applies to charge a non-resident if they are “carrying on a trade in the United Kingdom through a branch or agency” but in that case the non-resident is chargeable only on:

> “chargeable gains accruing on the disposal—

> (a) of assets situated in the United Kingdom and used in or for the purposes of the trade at or before the time when the capital [*sic*] gain accrued".

77. The question then is on our assumptions: are the assets disposed of "used in … a trade" before the time when the capital gain accrued? In a trade of property dealing in the UK by a non-resident the real property assets situated in the UK constitute the stock. Since stock is we think "used in … the trade" the assets disposed of are within s 10(1)(a) TCGA.

78. But we think it may nevertheless be a somewhat pointless question. This is because in the ordinary case if the assets are stock of the trade then by the operation of ss 37 and 39 TCGA the gain would be likely to be nil (see *Drummond v HMRC* [2009] EWCA Civ 608 per Rimer LJ at [25]. This is the case even though the computation of the profits of the trade under Part 2 ITTOIA gives rise to a lower figure than a CGT computation because of the different treatment of certain legal fees and payments.

79. It follows then that even if there is a trade of property dealing carried on in the UK through a branch or agency there will be no chargeable gains to tax, and on no basis can the appellant be charged to CGT on chargeable gains in 2005-06 and 2006-07.

80. The conclusion we have reached that there is no liability to CGT for the years assessed skews the dynamics of the arguments presented by each side on the issue of trading. If there is no CGT then the appellant does not need to show that there is a liability to income tax which is lower which would replace the CGT liability. HMRC on the other hand would like to show that there is a liability to income tax, even though there must be concerns about whether the existing assessments would be sufficient to capture the income tax liability or alternatively whether a new assessment could be made now.

Income tax liability on a non-resident trading in the UK: domestic law

81. Before we consider the question whether there is a trade here, there is another question following on, in some respects, from the s 10 TCGA one: if there is a trade of property dealing, is it chargeable to *income tax* under s 6 ITTOIA. That section charges the profits of a trade if it is carried on by a non-resident wholly or partly in the UK. As all the assets of any trade are situated in the UK and the trade is carried on by the sale in the UK of those assets by contracts having effect under the law of England and Wales it follows that if there is a trade it is carried on in the UK. It is to be noted that s 6 ITTOIA, unlike s 10 TCGA, does not refer to a branch or agency or to (the more modern phrase) a PE.

Income tax liability on a non-resident trading in the UK: international law

82. However if the appellant is a resident of a country with which the UK has a double taxation treaty then the treaty may apply to override the wide proposition set out in §81. If the appellant was a resident of the USA for the purposes of the relevant treaty between the UK and the USA then the answer to the question whether any trade of dealing in land is taxable in the UK depends, it seems to us, on the relationship

between articles 7 and 13 of SI 2002/2848, the instrument giving effect in domestic law to the Convention of 24 July 2001 between the governments of the United Kingdom and the United States of America ("UK-US DTA").

83. By article ("art") 7(1) of the UK-US DTA:

> "The business profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein."

84. By art 13(1):

> "Gains derived by a resident of a Contracting State that are attributable to the alienation of real property situated in the other Contracting State may be taxed in that other State."

85. But by art 7(6):

> "Where business profits include items of *income* [our emphasis] that are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article."

86. Thus if "gains from the alienation of real property" are "income" for the purposes of the convention then article 13 takes precedence and no PE is required.

87. We do not feel the need to decide this question, nor do we have the ability to decide it without at least further research and arguments from the parties, requiring as it does consideration of the interpretation of the UK-US DTA and with it the OECD Model Agreement and possibly the Vienna Convention on the law of treaties (Vienna, 23 May 1969). We mention a few of the issues that would need to be considered.

88. In the USA capital gains are included in income – see s 61(a)(3) Internal Revenue Code 1986 (Title 26 USC):

> "§61. Gross income defined
>
> (a) General definition
>
> Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:
>
> …
>
> (3) Gains derived from dealings in property"

89. That this includes what would, in the United Kingdom, be regarded as capital gains can be seen from the seminal case in the US Supreme Court of *Eisner v Macomber*, 252 US 189 [1920][1] ("*Macomber*")

[1] *Macomber* was incidentally cited with approval by the House of Lords Appellate Committee in *CIR v Blott* 8 TC 101 in the speech of Viscount Haldane in an early example of citing cases from outside the

90. In *Macomber* Justice Pitney said at 207:

> ""Income may be defined as the gain derived from capital, from labor, or from both combined," provided it be understood to include profit gained through a sale or conversion of capital assets, …"

91. In the UK a trade of dealing in real property will in nearly all cases involve the alienation of real property, and would in this case. But it could be difficult to characterise the sales of property in such a trade as themselves being "items of income": that term is much easier to ascribe to things such as interest or dividends received by a financial trader such as a bank or an insurance company.

92. We note though that art 13 of the UK-US DTA is headed "Gains", but the equivalent article in the OECD Model is headed "Capital Gains". If art 13 of the UK-USA DTA were headed "Capital Gains" it would be much easier to conclude that it did not cover gains that were made in the course of a trade. The difference must be of some significance. We note from the US Department of the Treasury's Technical Explanation of the Convention[2] that the United States refers in the explanation of art 13 to income and not anywhere to capital gains. See for example the Commentary on art 13(4):

> "This paragraph limits the taxing jurisdiction of the State of source with respect to gains from the alienation of ships or aircraft operated in international traffic by the enterprise alienating the ship or aircraft, from containers used in international traffic, and from property (other than real property) pertaining to the operation or use of such ships, aircraft, or containers.
>
> Under paragraph 4, such *income* [our emphasis] is taxable only in the Contracting State in which the alienator is resident. Notwithstanding paragraph 3, the rules of this paragraph apply even if the *income* is attributable to a permanent establishment maintained by the enterprise in the other Contracting State."

93. And in relation to art 13(5):

> "Paragraph 5 grants to the State of residence of the alienator the exclusive right to tax gains from the alienation of property other than property referred to in paragraphs 1 through 4. For example, gain derived from shares (other than shares described in paragraphs 2 or 3), debt instruments and various financial instruments, may be taxed only in the State of residence, to the extent such *income* is not otherwise characterized as income taxable under another article (e.g., Article 10 (Dividends) or Article 11 (Interest))."

British Empire in UK tax appeals. In *Blott* the Judicial Committee of the House of Lords also referred to *Swan Brewery Company v The King* [1914] AC 231, a Privy Council case from Western Australia. That case was also cited with approval by the Supreme Court of the United States in *Macomber* (in the judgments of Justice Pitney and Justice Brandeis) an example of the more internationally minded constitution of the Court in an era before the influence of Justice Antonin Scalia on citation of non-US decisions began to hold sway.

[2] https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/teus-uk.pdf

94. The answer may depend whether “income” in art 7(6) has an autonomous meaning or must be construed by reference to domestic law, and if so, which state’s.

95. These provisions of the DTA pose a conundrum we do not feel called upon to answer nor have we the had the arguments which may have convinced us one way or the other, but should there be an appeal against our primary decision on CGT the issue may have to be addressed and we have delineated some of the knotty problems that may arise.

96. But what we have been doing is to consider the UK-US DTA on the assumption that the appellant was a resident of the USA for the purposes of the DTA in the two relevant years of assessment. If she was not, the position may still be that s 6(2) ITTOIA would apply so that the United Kingdom may be entitled to charge the profits to income tax even if there was no PE.

97. However if there is a liability to income tax for the tax years 2006-07 and 2007-08, questions also arise whether the assessments for those years which are under appeal can be employed to charge the profits of such a trade. We consider that issue when considering the validity of the assessments.

98. Before leaving this area we note from the Technical Commentary that art 13(6) was designed to ensure that the UK could apply s 10A TCGA to a US resident. We also note that the UK/USA DTA does not prevent the US taxing the gains and in that case the UK must give credit for the US tax, but there is no suggestion in this case that the appellant has paid US income tax on the gains.

Recapitulation of our conclusions so far

99. Pulling together all the strings of the matters we have discussed above:

(1) we have found that the appellant was not resident in the United Kingdom for the year of assessment 2006-07,

(2) we have found that the appellant was not resident in the United Kingdom for the year of assessment 2007-08 or for that tax year (this term being the relevant one for the same concept for income tax but not CGT),

(3) we have found that the appellant was not ordinarily resident in the United Kingdom for the year of assessment 2006-07,

(4) we have found that the appellant was not ordinarily resident in the United Kingdom for the year of assessment 2007-08 or for that tax year,

(5) we have found that s 10A(1) TCGA applies in the case of the appellant,

(6) we have found that “the year of return” in which any gains falling within s 10A(2) are chargeable is 2008-09, a year of assessment for which no assessment to CGT has been made on the appellant,

(7) we have found that in any case s 10A(3) applies to exclude the chargeable gains made by the appellant from the gains that are taken into account under s 10A(2),

(8) the appellant therefore has no liability to CGT for 2006-07, 2007-08 or 2008-09,

(9) we consider, tentatively because we have not had argument on this point, that s 10 TCGA 1992 does not avail HMRC as an alternative way of charging the any gains. Section 10 can only apply at all if the appellant was carrying on a trade through a branch or agency in the UK and the gains arose from assets used in the trade. We can see no evidence of a branch or agency but we would probably find that the assets were used in the trade,

(10) but even if there were a branch or agency and the assets were used in the trade, we find that any CGT liability would be nil, by virtue of ss 37 and 39 TCGA (exclusion of receipts and expenses otherwise brought into account),

(11) our findings on CGT reverse the interests of the parties in arguing for there being trading or no trading for the purposes of income tax,

(12) if there is a trade of property dealing, the appellant as a non-resident is liable to income tax if the trade is carried on the UK (s 6 ITTOIA). We find that if there is a trade, it was so carried on,

(13) but without argument on the point, we are not able to come to a definitive conclusion whether art 7 of the UK-US DTA prevents an income tax charge arising on the grounds that the appellant had no PE in the UK. We would probably find that she had no such PE, but we are unable to decide whether art 13 of the UK-US DTA would help HMRC,

(14) and we have assumed without any finding to that effect that the appellant was a resident of the USA for the purposes of the UK-US DTA in the two relevant years of assessment. If she was not the position may still be that s 6(2) ITTOIA would apply.

Discussion: trading or investment?

100. Because the question of trading or not is not entirely moot and because we heard full argument on the point we now address it.

101. Mr Baptiste’s primary submission was that the appellant’s activities in buying and selling properties amounted to trading.

102. He submitted that her activities show all the hallmarks of a trade and referred to the “badges of trade” including the profit motive, the number of similar transactions and the same type of transactions.

103. He also argued that the fact that the properties had been held for up to three years was irrelevant as the important factor was the “trading cycle” which was relatively

long. The fact that there were no significant improvement works was also irrelevant – a trader does not have to add value to that which they sell, for example a car dealer.

104.He accepted that it was necessary for there to be an intention to trade from the outset. He referred to his letter of 10 November 2015 which he said contained the appellant's own words to the effect that she bought the properties with the intention of selling them on and that they were empty for long periods. She had also said that improvement works were done to one property.

105.He also referred to the statement in that letter that the appellant had a "property trading business account" with Lloyds TSB.

106.For HMRC Mrs Levy argued that no satisfactory evidence has been provided to show that the transactions were trading transactions. They pointed to the following matters as support for the proposition that there was no trading:

> (1) the first intimation that there was a trade was in the accountant's letter of 24 March 2015 even though the enquiry began in February 2013, and the notion of trading was, they suggested, only thought up when HMRC issued CGT calculations,
>
> (2) the 2006-07 return showed no trading income or any mention of a trade. Nor had the trade been notified in any earlier year although it was said to have started in 2003,
>
> (3) the facts that no improvements works were carried out and that the properties were not sold shortly after acquisition belied the notion of trading,
>
> (4) the properties were rented out which was also not indicative of trading,
>
> (5) the properties were apparently only sold because of the need for funds to meet the legal and other costs of the court case over the failed purchase, and
>
> (6) no details of the "trading" bank account have been provided.

107.She added that if the appellant was nonetheless found to be trading the legal fees would need to be shown to be deductible in accordance with s 54 Income Tax (Trading and Other Income) Act 2005 ("ITTOIA"). This must be an error as s 54 refers to interest and penalties charged under provisions of the taxation statutes.

108.HMRC cited two tax cases. They were:

> (1) *Lionel Simmons Properties Ltd (in liquidation) and others v Commissioners of Inland Revenue* 53 TC 461 ("*Lionel Simmons*") for the proposition of Lord Wilberforce at 491g that:
>
>> "One must ask, first, what the Commissioners were required or entitled to find. Trading requires an intention to trade: normally the question to be asked is whether this intention existed at the time of the acquisition of the asset. Was it acquired with the intention of disposing of it at a profit, or was it acquired as a permanent investment? Often it is

> necessary to ask further questions: a permanent investment may be sold in order to acquire another investment thought to be more satisfactory; that does not involve an operation of trade, whether the first investment is sold at a profit or at a loss. Intentions may be changed. What was first an investment may be put into the trading stock - and, I suppose, vice versa. If findings of this kind are to be made precision is required, since a shift of an asset from one category to another will involve changes in the company's accounts, and, possibly, a liability to tax."

(2) *Marson (HM Inspector of Taxes) v Morton and others* 59 TC 381 ("*Morton*") where Sir Nicholas Browne-Wilkinson V-C said at 392:

> "I believe that in order to reach a proper factual assessment in each case it is necessary to stand back, having looked at those matters, and look at the whole picture and ask the question - and for this purpose it is no bad thing to go back to the words of the statute - was this an adventure in the nature of trade? In some cases perhaps more homely language might be appropriate by asking the question, was the taxpayer investing the money or was he doing a deal?"

109. The quotation from *Morton* cited by HMRC comes immediately after the Vice-Chancellor had gone through the badges of trade, the things relied on by Mr Baptiste. We therefore consider the position in this case (in italics) in relation to the issues discussed by the Vice-Chancellor.

(1) Is the transaction in question [ ] a one-off transaction? Although a one-off transaction is in law capable of being an adventure in the nature of trade, obviously the lack of repetition is a pointer which indicates there might not here be trade but something else.

Here there is one element of repetition: the appellant has said that she sold one of the properties to buy another.

(2) Is the transaction in question in some way related to the trade which the taxpayer otherwise carries on? For example, a one-off purchase of silver cutlery by a general dealer is much more likely to be a trade transaction than such a purchase by a retired colonel.

Here there is no other related trade.

(3) The nature of the subject matter may be a valuable pointer. Was the transaction in a commodity of a kind which is normally the subject matter of trade and which can only be turned to advantage by realisation, such as referred to in the passage that the Chairman quoted from *Reinhold*? For example, a large bulk of whisky or toilet paper is essentially a subject matter of trade, not of enjoyment.

Real property is one of those kinds of asset where its nature is no pointer to whether it is held for investment or as trading stock. Such property may yield an income or growth in value or both.

(4) In some cases attention has been paid to the way in which the transaction was carried through: was it carried through in a way typical of the trade in a commodity of that nature?

There is no evidence to suggest that a property dealer would not carry out transactions in the way the appellant did.

(5) What was the source of finance of the transaction? If the money was borrowed that is some pointer towards an intention to buy the item with a view to its resale in the short term; a fair pointer towards trade.

Finance was raised by way of mortgage loan.

(6) Was the item which was purchased resold as it stood or was work done on it or relating to it for the purposes of resale? For example, the purchase of second-hand machinery which was repaired or improved before resale. If there was such work done, that is again a pointer towards the transaction being in the nature of trade.

HMRC have added that no "development work" was done. The appellant has said that some work was done on some properties but it is not clear whether it was normal repair work or more substantial improvement.

(7) Was the item purchased resold in one lot as it was bought, or was it broken down into saleable lots? If it was broken down it is again some indication that it was a trading transaction, the purchase being with a view to resale at profit by doing something in relation to the object bought.

There was no breaking down (and we do not know of that was even possible).

(8) What were the purchasers' intentions as to resale at the time of purchase? If there was an intention to hold the object indefinitely, albeit with an intention to make a capital profit at the end of the day, that is a pointer towards a pure investment as opposed to a trading deal. On the other hand, if before the contract of purchase is made a contract for resale is already in place, that is a very strong pointer towards a trading deal rather than an investment. Similarly, an intention to resell in the short term rather than the long term is some indication against concluding that the transaction was by way of investment rather than by way of a deal. However, as far as I can see, this is in no sense decisive by itself.

The appellant says the intention was to trade by reference to the property cycle and that this explains why most of the properties were held for three years or so. HMRC point out that the sale of some was a forced sale (to raise funds for legal costs) and the appellant agrees that the cycle referred to had not reached the stage where sale was desirable.

(9) Did the item purchased provide enjoyment for the purchaser (for example, a picture), or pride of possession, or produce income pending resale? If it did, then that may indicate an intention to buy either for personal satisfaction or to invest for income yield, rather than do a deal purely for the purpose of making a profit on the turn. I will consider in a moment the question whether, if there is

> no income produced or pride of possession pending resale, that is a strong pointer in favour of it being a trade rather than an investment.
>
> *The properties all seem to have been rented out for some periods though the appellant says they were empty for period before sale. There is no enjoyment in the sense of occupying the properties as a residence.*

110. Having considered all the evidence and the submissions of the parties, and having in mind the quotation from the decision of the Vice-Chancellor in §108(2), we find that on the balance of probabilities there is no trade of property dealing carried on by the appellant. The appellant was investing her money, not doing deals. We say this for the following reasons:

111. Badges 1, possibly 2, 6 and importantly 8 are against the appellant

112. Badges 3, 7 and 9 are neutral. We also think that in the context of let property Badge 5 is neutral.

113. Badge 4 is in the appellant's favour but we think it is not a very important point in the context of this purported trade.

114. As to matters raised apart from the badges, without further evidence such as the information given to the bank when the account was opened, we cannot accept the mere naming of an account as "trading" is proof that that was what it was used for. Banks, as is well known, distinguish between personal accounts and business accounts. Whether Lloyds TSB make a case by case determination of the intended use of an account before allowing it to be named a "trading" as distinct from a "business" account we do not know and have no evidence about the matter. Whether they even determine or care what a business account is called by the account holder we do not know and we have no evidence of their practice.

115. We are also influenced by the fact that, as HMRC point out vigorously, there is no hint or suggestion in the papers that the dealings in real property were considered to be a trade until February 2015. We very much doubt if trading would have been suggested were it not for the appellant's (or, rather Mr Baptiste's) realisation that £106,000 or so in outlays may be deductible in arriving at a trading profit but are not deductible in a chargeable gains computation.

116. These two matters cast a lot of doubt on the notion that in 2003 the appellant had the intention of trading in property (as required by *Lionel Simmons*) rather than buying to let with the possibility of selling at the right price. Real property is notoriously an asset which may yield a return from allowing another to occupy it for a rent or from making a gain on sale. The latter will often amount to trading if there is a quick turnaround based on a refurbishment of a property acquired at a bargain price often at auction, but that is not the case here.

Discussion: the deductions

117. In case we may be found to have committed an error of law in making the finding we did that there was no trade, we add here our views on the question of the

deductions claimed by the appellant in arriving at the trading profit (and also for the purposes of TCGA 1992). The deductibility of the expense had been put in issue by HMRC.

118.The trading accounts put forward by Baptiste & Co included a deduction of £10,600 "lost deposit" in 2004-05 and £95,951 of legal fees in 2006-07. These included a payment of £42,500 which appears to be damages awarded against the appellant.

119.The circumstances in which these payments were made are not entirely clear from the voluminous documentation. It appears that the appellant or possibly her solicitors acting without her instructions put a deposit of £10,600 on a property with a view to purchasing it. For some reason, perhaps connected with the lack of instructions, the appellant did not complete on the property and so forfeited her deposit.

120.Had the intention been to acquire the property as part of a trading portfolio, which is what the appellant maintains, then we would certainly accept that the lost deposit was a "loss … connected with or arising out of the trade" and so not disallowed by s 34(1)(b) ITTOIA.

121.We assume that the payment of damages in 2006-07 was to compensate the vendors for losses they may have incurred when not able to sell the property. The papers show that the appellant was a Part 20 defendant in an action by (we assume) the vendors. We consider that this payment was also a loss that would not be disallowed by s 34(1)(b) ITTOIA.

122.The legal fees incurred by the appellant are also in our view deductible in arriving at the profits of the trade being incurred wholly and exclusively for the purposes of the trade.

123.As to the CGT computation, a forfeited deposit may be treated as giving rise to an allowable loss by s 144(7) TCGA which equates forfeited deposits with abandoned options. But s 144(4) restricts the creation of an allowable loss on abandonment to cases where the person losing the deposit intended to use the asset concerned "for the purpose of a trade carried on by" them. In the case of land we can see that but for this limitation anyone who lost a deposit when trying to acquire a property to be used as their principal private residence would be able to claim a loss. But it is difficult to see why a person intending to let the property by way of business should not be able to claim: but the answer may be that that distinction would be difficult to police, whereas with trade premises it will be obvious that it was not a residence. The outcome is that no deduction may be given for CGT purposes.

124.Neither the lost deposit, the damages nor the legal fees fall within s 38 TCGA. To so fall the expenses must have been incurred on an asset which is disposed of and there was none here. There is no relief for abortive expenditure where no asset is acquired.

Discussion: the discovery assessments

125.In view of what we have held about the chargeable gains this issue also becomes moot. We consider it in case we may be shown to be wrong about s 10A TCGA and as we heard argument.

126.HMRC accepted that the burden of proof was on them to show that the discovery assessments had been properly raised and that there was carelessness that brought about a loss of tax.

127.HMRC argued that:

(1) the assessments for 2006-07 and 2007-08 to CGT were correct as they reflected the property sales which were the sales of investments, not of trading stock,

(2) the discovery assessments were properly made as they had discovered a loss of tax in each year, namely that chargeable gains which ought to have been assessed had not been assessed,

(3) the loss of tax was brought about carelessly thus justifying the assessments being made after the normal 4 year time limit but before the 6 year limit. A reasonable taxpayer exercising reasonable diligence would have included the gains on their 2006-07 return and would have made a return in 2007-08 to include the gains, and

(4) in the two years concerned, s 10A TCGA 1992 made her chargeable on any gains even though she spent time outside the UK in those years.

128.In the case of both years HMRC have the burden of showing that there was in the reasonable opinion of the officer of HMRC a loss of tax. We consider they have met that burden. The information available to the officer from sources outside the return showed that gains were likely to have been made on the disposal of at least three properties, gains which for 2006-07 had been omitted from the return and for 2007-08 had not been shown because no return was made. The fact that we have held that the officer was wrong to think that gains arose in the years concerned by virtue of s 10A because he misunderstood the way that section worked is we think irrelevant. In s 29(1) TMA the test is subjective.

129.For 2006-07 HMRC had to show that the loss of tax was brought about carelessly or deliberately or alternatively fell within the provisions of s 29(5) TMA. As the timing of the discovery meant that only careless conduct or worse could justify making an assessment at all (by virtue of s 36(1) TMA), it was s 29(4) that was relied on. For 2007-08 section 29(4) or (5) did not apply as no return had been made, but because of the time limit issues s 36(1) TMA also required carelessness to be shown for that year.

130.Section 118(5) TMA provides that:

> "For the purposes of this Act a loss of tax or a situation is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss or situation."

131.In our view HMRC have not shown on the balance of probabilities that the appellant was careless within the meaning of that section. For 2006-07 she indicated in her return that she was non-resident. She was entitled to think that she had no liability to CGT for that year. It might be argued that she should have made enquiries from, for example, Mr Baptiste or HMRC as to the effect of a period of non-residence, but there is no reason to think that had she done so she would not have been told that s 10A(3) TCGA would protect her from CGT in respect of assets acquired in years of departure or non-residence or that she would not have been told that even without s 10A(3) she should not return any gains in 2006-07 or 2007-08, but in the year of return.

132.We should mention one other small point. When the 2006-07 protective assessment was made it included a figure of £7,000 on which the tax was £196.50. The letter preceding the assessment referred to HMRC being in possession of information about rents received by her. To the extent then that the discovery assessment was made to recover this tax loss of which HMRC was newly aware it was properly made for the purposes of s 29(1).

133.Because income from property is always taxable irrespective of a person's residence status it was in our view careless of the appellant to omit it from her returns. The discovery assessment is therefore justified in relation to this income. But this small amount does not we think act as a peg, or jumping off point, to justify the much larger CGT assessment. We think that s 29(1) TMA must be considered separately in relation to each source at least as far as income and chargeable gains are concerned. We have also noted that for reasons we do not understand the rental income was omitted from the amended assessment, perhaps because of more accurate information coming to HMRC's attention or perhaps from an oversight.

134.For 2007-08 we assume that had a return been made it would also have claimed non-residence status and the same view as to CGT could have been legitimately taken.

135.But as we have said even if carelessness had been shown it and the assessments justified it would have availed HMRC nothing as any chargeable gains that there might have been were taxable only in 2008-09.

136.Had we found that the assessments were justified and that there was an income tax liability from a trade of property dealing we are inclined to think that the assessments could not be varied to include the profits of that trade. That would undoubtedly be a harsh result for HMRC because the issue was only raised by the appellant at a time when an assessment could only have been made on the basis that HMRC could show deliberate conduct by her in omitting or not earning the profits. We do not need to come to a definitive conclusion on this point.

Discussion: penalties

137.HMRC say that the penalties were correctly imposed for the same reason as the discovery assessments, negligent behaviour (the requirement in s 93(5) and s 95 TMA) being the same as careless behaviour.

138.They also say that the level of penalty at 40%, reduced from an initial 60%, was fair having regard to HMRC's published policy on abatement.

139.In view of what we have said above about gains, trading and discovery assessments the issue of penalties is also moot.

140.But we say in any case that we can see no reason to differ from the HMRC calculation of the abatement that would apply if carelessness had been shown.

Decision

141.In accordance with s 50(6)(c) TMA we reduce the assessment to income tax and CGT for the year of assessment 2006-07 to nil.

142.In accordance with s 50(6)(c) TMA we reduce the assessment to CGT for the year of assessment 2007-08 to nil.

143.In accordance with s 100B(2)(b)(i) TMA we set aside the determination of the penalty under s 95(1) TMA for the year of assessment 2006-07.

144.In accordance with s 100B(2)(b)(i) TMA we set aside the determination of the penalty under s 93(5) TMA for the year of assessment 2007-08.

145.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.

RICHARD THOMAS
TRIBUNAL JUDGE

RELEASE DATE: 19 APRIL 2017

APPENDIX 1

TAXATION OF CHARGEABLE GAINS ACT 1992

2 Persons and gains chargeable to capital gains tax, and allowable losses

(1) Subject to any exceptions provided by this Act, and without prejudice to sections 10 and 276, a person shall be chargeable to capital gains tax in respect of chargeable gains accruing to him in a year of assessment during any part of which he is resident in the United Kingdom, or during which he is ordinarily resident in the United Kingdom.

10 Non-resident with United Kingdom branch or agency

(1) Subject to any exceptions provided by this Act, a person shall be chargeable to capital gains tax in respect of chargeable gains accruing to him in a year of assessment in which he is not resident and not ordinarily resident in the United Kingdom but is carrying on a trade in the United Kingdom through a branch or agency, and shall be so chargeable on chargeable gains accruing on the disposal—

> (a) of assets situated in the United Kingdom and used in or for the purposes of the trade at or before the time when the capital gain accrued, or
>
> (b) of assets situated in the United Kingdom and used or held for the purposes of the branch or agency at or before that time, or assets acquired for use by or for the purposes of the branch or agency.

(2) Subsection (1) above does not apply unless the disposal is made at a time when the person is carrying on the trade in the United Kingdom through a branch or agency.

(6) In this Act, unless the context otherwise requires, "branch or agency" means any factorship, agency, receivership, branch or management, but does not include any person within the exemptions in section 82 of the Management Act (general agents and brokers).

10A Temporary non-residents

(1) This section applies in the case of any individual ("the taxpayer") if—

> (a) he satisfies the residence requirements for any year of assessment ("the year of return");
>
> (b) he did not satisfy those requirements for one or more years of assessment immediately preceding the year of return but there are years of assessment before that year for which he did satisfy those requirements;
>
> (c) there are fewer than five years of assessment falling between the year of departure and the year of return; and

(d) four out of the seven years of assessment immediately preceding the year of departure are also years of assessment for each of which he satisfied those requirements.

(2) Subject to the following provisions of this section …, the taxpayer shall be chargeable to capital gains tax as if—

(a) all the chargeable gains and losses which (apart from this subsection) would have accrued to him in an intervening year,

…

were gains or, as the case may be, losses accruing to the taxpayer in the year of return.

(3) Subject to subsection (4) below, the gains and losses which by virtue of subsection (2) above are to be treated as accruing to the taxpayer in the year of return shall not include any gain or loss accruing on the disposal by the taxpayer of any asset if—

(a) that asset was acquired by the taxpayer at a time in the year of departure or any intervening year when--

(i) he was neither resident nor ordinarily resident in the United Kingdom, or

(ii) he was resident or ordinarily resident in the United Kingdom but was Treaty non-resident;

…

(5) The gains and losses which by virtue of subsection (2) above are to be treated as accruing to the taxpayer in the year of return shall not include any chargeable gain or allowable loss accruing to the taxpayer in an intervening year which, in the taxpayer's case, has fallen to be brought into account for that year by virtue of section 10 or 16(3).

(7) Where this section applies in the case of any individual, nothing in any enactment imposing any limit on the time within which an assessment to capital gains tax may be made shall prevent any such assessment for the year of departure from being made in the taxpayer's case at any time before the end of two years after the 31st January next following the year of return.

(8) In this section—

"intervening year" means any year of assessment which, in a case where the conditions in paragraphs (a) to (d) of subsection (1) above are satisfied, falls between the year of departure and the year of return;

> “relevant disposal”, means a disposal of an asset acquired by the person making the disposal at a time when that person was resident or ordinarily resident in the United Kingdom and was not Treaty non-resident; and
>
> “the year of departure” means the last year of assessment before the year of return for which the taxpayer satisfied the residence requirements.

(9) For the purposes of this section an individual satisfies the residence requirements for a year of assessment—

> (a) if, during any part of that year of assessment, he is resident in the United Kingdom …, or
>
> (b) if he is ordinarily resident in the United Kingdom during that year of assessment, ….

…

(9C) Nothing in any double taxation relief arrangements shall be read as preventing the taxpayer from being chargeable to capital gains tax in respect of any of the chargeable gains treated by virtue of subsection (2)(a) above as accruing to the taxpayer in the year of return (or as preventing a charge to that tax from arising as a result).

37 Consideration chargeable to tax on income

(1) There shall be excluded from the consideration for a disposal of assets taken into account in the computation of the gain any money or money’s worth charged to income tax as income of, or taken into account as a receipt in computing income or profits or gains or losses of, the person making the disposal for the purposes of the Income Tax Acts.

38 Acquisition and disposal costs etc

(1) Except as otherwise expressly provided, the sums allowable as a deduction from the consideration in the computation of the gain accruing to a person on the disposal of an asset shall be restricted to—

> (a) the amount or value of the consideration, in money or money’s worth, given by him or on his behalf wholly and exclusively for the acquisition of the asset, together with the incidental costs to him of the acquisition or, if the asset was not acquired by him, any expenditure wholly and exclusively incurred by him in providing the asset,
>
> (b) the amount of any expenditure wholly and exclusively incurred on the asset by him or on his behalf for the purpose of enhancing the value of the asset, being expenditure reflected in the state or nature of the asset at the time of the disposal, and any expenditure wholly and exclusively incurred by him in establishing, preserving or defending his title to, or to a right over, the asset,

(c) the incidental costs to him of making the disposal.

(2) For the purposes of this section and for the purposes of all other provisions of this Act, the incidental costs to the person making the disposal of the acquisition of the asset or of its disposal shall consist of expenditure wholly and exclusively incurred by him for the purposes of the acquisition or, as the case may be, the disposal, being fees, commission or remuneration paid for the professional services of any surveyor or valuer, or auctioneer, or accountant, or agent or legal adviser and costs of transfer or conveyance (including stamp duty or stamp duty land tax) together—

(a) in the case of the acquisition of an asset, with costs of advertising to find a seller, and

(b) in the case of a disposal, with costs of advertising to find a buyer and costs reasonably incurred in making any valuation or apportionment required for the purposes of the computation of the gain, including in particular expenses reasonably incurred in ascertaining market value where required by this Act.

(3) Except as provided by section 40, no payment of interest shall be allowable under this section.

39 Exclusion of expenditure by reference to tax on income

(1) There shall be excluded from the sums allowable under section 38 as a deduction in the computation of the gain any expenditure allowable as a deduction in computing the profits or losses of a trade, profession or vocation for the purposes of income tax or allowable as a deduction in computing any other income or profits or gains or losses for the purposes of the Income Tax Acts and any expenditure which, although not so allowable as a deduction in computing any losses, would be so allowable but for an insufficiency of income or profits or gains; and this subsection applies irrespective of whether effect is or would be given to the deduction in computing the amount of tax chargeable or by discharge or repayment of tax or in any other way.

(2) Without prejudice to the provisions of subsection (1) above, there shall be excluded from the sums allowable under section 38 as a deduction in the computation of the gain any expenditure which, if the assets, or all the assets to which the computation relates, were, and had at all times been, held or used as part of the fixed capital of a trade the profits of which were (irrespective of whether the person making the disposal is a company or not) chargeable to income tax would be allowable as a deduction in computing the profits or losses of the trade for the purposes of income tax.

144 Options and forfeited deposits

(1) Without prejudice to section 21, the grant of an option, and in particular—

(a) the grant of an option in a case where the grantor binds himself to sell what he does not own, and because the option is abandoned, never has occasion to own, and

(b) the grant of an option in a case where the grantor binds himself to buy what, because the option is abandoned, he does not acquire,

is the disposal of an asset (namely of the option), but subject to the following provisions of this section as to treating the grant of an option as part of a larger transaction.

…

(4) The abandonment of—

…

(c) an option to acquire assets exercisable by a person intending to use them, if acquired, for the purpose of a trade carried on by him,

shall constitute the disposal of an asset (namely of the option); but the abandonment of any other option by the person for the time being entitled to exercise it shall not constitute the disposal of an asset by that person.

(7) This section shall apply in relation to a forfeited deposit of purchase money or other consideration money for a prospective purchase or other transaction which is abandoned as it applies in relation to the consideration for an option which binds the grantor to sell and which is not exercised.

APPENDIX 2

INCOME (TRADING AND OTHER INCOME ACT 2005

5 Charge to tax on trade profits

Income tax is charged on the profits of a trade, profession or vocation.

6 Territorial scope of charge to tax

(1) Profits of a trade arising to a UK resident are chargeable to tax under this Chapter wherever the trade is carried on.

(2) Profits of a trade arising to a non-UK resident are chargeable to tax under this Chapter only if they arise—

(a) from a trade carried on wholly in the United Kingdom, or

(b) in the case of a trade carried on partly in the United Kingdom and partly elsewhere, from the part of the trade carried on in the United Kingdom.

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.

APPENDIX 3

TAXES MANAGEMENT ACT 1970

29 Assessment where loss of tax discovered

(1) If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment—

(a) 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

…

the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, 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.

…

(3) Where the taxpayer has made and delivered a return under section 8 … of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above—

(a) in respect of the year of assessment mentioned in that subsection; and

(b) ... in the same capacity as that in which he made and delivered the return,

unless one of the two conditions mentioned below is fulfilled.

(4) The first condition is that the situation mentioned in subsection (1) above was brought about carelessly … by the taxpayer or a person acting on his behalf.

…

(8) An objection to the making of an assessment under this section on the ground that neither of the two conditions mentioned above is fulfilled shall not be made otherwise than on an appeal against the assessment.

(9) Any reference in this section to the relevant year of assessment is a reference to—

(a) in the case of the situation mentioned in paragraph (a) or (b) of subsection (1) above, the year of assessment mentioned in that subsection; and

(b) in the case of the situation mentioned in paragraph (c) of that subsection, the year of assessment in respect of which the claim was made.

36 Loss of tax brought about carelessly or deliberately etc

(1) An assessment on a person in a case involving a loss of income tax or capital gains tax brought about carelessly by the person may be made at any time not more than 6 years after the end of the year of assessment to which it relates (subject to … any other provision of the Taxes Acts allowing a longer period).

…

(1B) In subsection[(1)] …, references to a loss brought about by the person who is the subject of the assessment include a loss brought about by another person acting on behalf of that person.

…

93 Failure to make return for income tax and capital gains tax

(1) This section applies where—

(a) any person (the taxpayer) has been required by a notice served under or for the purposes of section 8 … of this Act ... to deliver any return, and

(b) he fails to comply with the notice.

(5) … if—

(a) the failure by the taxpayer to comply with the notice continues after the anniversary of the filing date, and

(b) there would have been a liability to tax shown in the return,

the taxpayer shall be liable to a penalty of an amount not exceeding the liability to tax which would have been so shown.

(9) References in this section to a liability to tax which would have been shown in the return are references to an amount which, if a proper return had been delivered on the filing date, would have been payable by the taxpayer under section 59B of this Act for the year of assessment.

(10) In this section--

“the filing date” in respect of a return for a year of assessment (Year 1) means—

(a) 31st January of Year 2, or

(b) if the notice under section 8 … was given after 31st October of Year 2, the last day of the period of three months beginning with the day on which the notice is given.

“the period of default”, in relation to any failure to deliver a return, means the period beginning with the filing date and ending with the day before that on which the return was delivered.,

95 Incorrect return or accounts for income tax or capital gains tax

(1) Where a person fraudulently or negligently—

(a) delivers any incorrect return of a kind mentioned in or either of those sections as extended by section 12 of this Act ...

…

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; …

100 Determination of penalties by officer of Board

(1) Subject to subsection (2) below and except where proceedings for a penalty have been instituted under section 100D below ..., an officer of the Board authorised by the Board for the purposes of this section may make a determination imposing a penalty under any provision of the Taxes Acts and setting it at such amount as, in his opinion, is correct or appropriate.

(3) Notice of a determination of a penalty under this section shall be served on the person liable to the penalty and shall state the date on which it is issued and the time within which an appeal against the determination may be made.

(4) After the notice of a determination under this section has been served the determination shall not be altered except in accordance with this section or on appeal.

(5) If it is discovered by an officer of the Board authorised by the Board for the purposes of this section that the amount of a penalty determined under this section is or has become insufficient the officer may make a determination in a further amount so that the penalty is set at the amount which, in his opinion, is correct or appropriate.

100B Appeals against penalty determinations

(1) An appeal may be brought against the determination of a penalty under section 100 above and, subject to ...the following provisions of this section, the provisions of this Act relating to appeals shall have effect in relation to an appeal against such a determination as they have effect in relation to an appeal against an assessment to tax except that references to the tribunal shall be taken to be references to the First-tier Tribunal.

(2) On an appeal against the determination of a penalty under section 100 above section 50(6) to (8) of this Act shall not apply but—

(a) in the case of a penalty which is required to be of a particular amount, the First-tier Tribunal may--

(i) if it appears ... that no penalty has been incurred, set the determination aside,

(ii) if the amount determined appears ... to be correct, confirm the determination, or

(iii) if the amount determined appears ... to be incorrect, increase or reduce it to the correct amount,

(b) in the case of any other penalty, the First-tier Tribunal may—

(i) if it appears ... that no penalty has been incurred, set the determination aside,

(ii) if the amount determined appears ... to be appropriate, confirm the determination,

(iii) if the amount determined appears ... to be excessive, reduce it to such other amount (including nil) as it considers appropriate, or

(iv) if the amount determined appears ... to be insufficient, increase it to such amount not exceeding the permitted maximum as it considers appropriate.

103 Time limits for penalties

(1) Subject to subsection (2) below, where the amount of a penalty is to be ascertained by reference to tax payable by a person for any period, the penalty may be determined

by an officer of the Board, or proceedings for the penalty may be commenced before the tribunal or a court—

(a) at any time within six years after the date on which the penalty was incurred, or

(b) at any later time within three years after the final determination of the amount of tax by reference to which the amount of the penalty is to be ascertained.

118 Interpretation

(5) For the purposes of this Act a loss of tax or a situation is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss or situation.

(6) Where—

(a) information is provided to Her Majesty's Revenue and Customs,

(b) the person who provided the information, or the person on whose behalf the information was provided, discovers some time later that the information was inaccurate, and

(c) that person fails to take reasonable steps to inform Her Majesty's Revenue and Customs,

any loss of tax or situation brought about by the inaccuracy shall be treated for the purposes of this Act as having been brought about carelessly by that person.