[2017] UKFTT 0658 (TC)

TC06085

Appeal number: TC/2016/03838

CAPITAL GAINS TAX – principal private residence relief - short period of occupation - whether property was appellant's "home" -nature of occupation- discovery assessments and time limits - burden of proof.

FIRST-TIER TRIBUNAL
TAX CHAMBER

STEPHEN BAILEY **Appellant**

- and -

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

TRIBUNAL: JUDGE MARILYN MCKEEVER

Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 18 August 2017

Mr Richard Baptiste, accountant, for the Appellant

Mrs Bisi Sanu, presenting officer, for the Respondents

DECISION

Preliminary matters

1. This case concerns an assessment to Capital Gains Tax for the tax year 2010-11 on the disposal of a property known as "Richmond" in Farnham Surrey ("Richmond") and whether the Appellant is entitled to principal private residence relief in respect of it.

2. An assessment in respect of Capital Gains Tax ("CGT") of £27,312 was issued on 26 February 2016 under section 29 Taxes Management Act 1970 ("TMA")-a "discovery assessment". This replaced an earlier closure notice which had been issued on 23 April 2015 under section 28A(1) and (2) TMA. We return to these procedural matters later.

3. A penalty assessment notice was originally issued on 26 June 2015 under Schedule 24 Finance Act 2007, with the penalty of £19,118.40 calculated by reference to "deliberate" behaviour. This was replaced by a notice of amended penalty assessment, in the same amount, on 13 May 2016, following the issue of the discovery assessment.

4. A penalty of £300 for failure to comply with an Information Notice under paragraph 39 and 46 of Schedule 36 Finance Act 2008 was also issued on 1 July 2014.

5. Although the Appellant's appeal to HMRC was not in the bundle, HMRC's letter of 3 March 2016 to Mr Batiste, which enclosed the discovery assessment, stated "you appealed agains my decision to raise a charge for Capital Gains Tax in the 2010-11 tax period and to charge a penalty.This appeal has been accepted and has been noted on Mr Bailey's records." There does not appear to have been a separate appeal against the revised assessment and penalty assessment and we infer that HMRC regarded the original appeal as applying to the replacements and will treat that as being the case.

6. The appeal to the Tribunal was made late on 15 July 2016 but HMRC did not raise the point and fully presented their case. I consider that it is in the interests of justice for the case to proceed and give permission for the appeal to be made out of time.

7. Although the appeal to HMRC was against both the CGT and the penalty, the notice of appeal to the Tribunal refers only to the CGT.

8. Mr Baptiste had not submitted a witness statement for Mr Bailey despite Directions issued by the Tribunal requiring any witness statements to be provided. However, it became clear in the course of the hearing that it would be helpful for Mr Bailey to be able to explain various matters and Mrs Sanu agreed that Mr Bailey should be able to give oral evidence, which he did.

The facts

9. I had before me an extensive bundle of documents and, as mentioned above, this was supplemented with oral evidence given by Mr Bailey. I found Mr Bailey to be an honest and reliable witness.

10. HMRC's computer records show that Mr Bailey's tax return for the year 2010-11 was submitted, in time, on 12 January 2012. The return did not declare any capital gains and no income tax was due as Mr Bailey had made losses on his property business.

11. HMRC opened an enquiry into the return on 12 March 2014 and requested information concerning the ownership and sale of property. The letter was sent to Mr Bailey and also to his representative, Mr Baptiste.

12. Under the Taxes Management Act 1970 ("TMA") HMRC have one year from the return filing date in which to open an enquiry into it; the "enquiry window". If an enquiry is not opened within the enquiry window, HMRC may be able to make a "discovery assessment", under section 29 TMA.

13. Where an enquiry is commenced within the enquiry window, an assessment may be made on the issue of a closure notice under section 28A(1) and (2) TMA. The April 2015 assessment was the result of a closure notice under this provision. However, the enquiry had been opened long after the enquiry window had closed and so the assessment could only be made as a discovery assessment under section 29 TMA. Realising their mistake, HMRC cancelled the original closure notice and issued the discovery assessment and that is the decision against which the Appellant has appealed.

14. HMRC requested information on various occasions from Mr Bailey and his representative, but there was no response from either. A formal information notice under schedule 36 Finance Act 2008 was issued on 17 April 2014. This was not complied with, despite reminders and the £300 penalty was issued on 1 July 2014. It appears there were some telephone calls from Mr Baptiste promising to provide the information, but no information was sent. The closure notice and penalty assessments were subsequently issued as described above. HMRC's warning letter of 10 March 2015 stated "As the omission from your return appears to have been a "Deliberate" decision to avoid paying the correct tax…a penalty determination will soon be issued to you.". There was no explanation as to why the inaccuracy was regarded as "deliberate".

15. In response to the 23 April 2015 assessment, Mr Baptiste wrote to HMRC claiming that no CGT was due on the basis that Mr Bailey was entitled to main residence relief under section 222 Taxation of Chargeable Gains Act 1992 ("TCGA") as he had moved into Richmond for a short time before it was sold. As he had owned the property for less than three years, the entire gain was exempt under section 223 TCGA as it was at the time. Mr Baptiste's letter (unhelpfully for his client's case) stated "Mr Bailey moved into the property in

May 2010 and did decorating, painting and landscaping himself with a view to selling the property."

16. The letter also explained that the property had previously been tenanted by a close friend of Mr Bailey. The friend died in February or March 2010 and we heard from Mr Bailey that the friend's widow continued to live there for a period but moved out. Mr Baptiste also stated that Mr Bailey suffered clinical depression following his friend's death which led to continuing mental health issues. HMRC asked for medical evidence about this but none was provided.

17. In evidence Mr Bailey said that as well as the mental health issues he had suffered from extremely high blood pressure and still had seizures. He had medical evidence from his doctor, but because of his mental health had been unable to deal with paperwork. I observe, without making any finding about Mr Bailey's mental state at the time, that my bundle of documents included a letter from Mr Bailey received by HMRC on 2 November 2015 which contained an extraordinary rant against HMRC and the officer concerned. It seemed to me to go beyond what might have been written by a rational but angry person. This letter was treated as an appeal.

18. Mr Baptiste put forward very little evidence regarding Mr Bailey's occupation of Richmond. There was a letter from Mr Bailey's solicitor who acted on the sale, addressed to him at Richmond and a document described as a "witness statement" signed by Mr Bailey's partner Ms Lynette Read signed and dated 24 March 2017 which simply stated "I Lynette Read confirm that Mr Stephen Bailey lived at Lower Bourne Farnham for a period of several months prior to selling the same property he lived in on 31 August 2010." Ms Read did not attend the hearing.

19. I found Mr Bailey's oral account of events more helpful and I accept his evidence, as set out below, as my findings of fact.

20. Mr Bailey was divorced. He had a successful property business. Mr Bailey's children were at school in Maidstone. The children lived with him and in order to be close to their school he and Ms Read bought a property in Tonbridge Road, Maidstone ("Maidstone") jointly. Ms Read's son also lived with them.

21. Ms Read worked in Ealing and had a property, which she owned, in Tachbrook Road, Feltham, Middlesex ("Tatchbrook"). Ms Read lived in the Tachbrook property during the week and in the Maidstone property at the weekend.

22. Richmond was originally acquired by Mr Bailey's company, Landseers Ltd in February 2008 for £420,000 with a three month bridging loan. In tandem with the company's purchase, Mr Bailey was obtaining a mortgage and he and Ms Read were looking to let the Maidstone property. The intention all along was that Richmond should be a home for the family. Mr Bailey moved some of the furniture from Maidstone into Richmond. He only moved the basics as the intention was to let Maidstone furnished. However, his children lived with him

and he and they lived in the property for two and a half months whilst he tried to sort out his financial arrangements. He intended to take out a normal mortgage, buy the property from the company (enabling the company to repay the bridging loan) and then live in Richmond, which he said was much nicer than Tachbrook, as a family home.

23. Mr Bailey could not remember what action he had taken at the time with regard to notifying people of his change of address etc, but given that all this happened nearly ten years ago, that is not surprising and I do not make any adverse inferences.

24. Mr Bailey's plans were then overtaken by the financial crash of 2008. It was impossible for him to obtain a normal mortgage. The only finance available was on a "buy-to-let" basis and under the terms of the mortgage he would be forbidden from living in the property. Mr Bailey accepted the buy-to-let mortgage as the alternative would have been for the company to have defaulted on the bridging loan which would have resulted in the property being repossessed by the lender.

25. Mr Bailey bought Richmond from Landseers on 2 May 2008 for £429,000 and let it in accordance with the terms of the mortgage. He then lived with Ms Read at Tatchbrook.

26. When Richmond's tenant died and his widow left, Mr Bailey moved into the property, again intending to make it a home for the family. The property required some painting and decorating and Mr Bailey commenced this while living there to get the house ready for the family to move in with him.

27. However, within the first couple of weeks of occupation, Mr Bailey realised that because of his mental state he was unable to cope with living in the house and he decided to sell it. He carried on with the decorating etc and sold the house on 31 August 2010 for £550,000 realising a gain of £121,000.

28. The gain should have been included in Mr Bailey's 2010-11 tax return and a claim for main residence relief made in the return. However, the gain was omitted altogether.

The Appellant's submissions

29. Mr Baptiste submitted that Mr Bailey was entitled to main residence relief on the whole of the gain so no CGT is due.

30. Although there was no specific appeal against the Schedule 24 Finance Act 2007 penalties, as they are linked to the tax due, it would follow that the penalty would fall away if he were successful.

The Respondent's submissions

31. There was no evidence to show that Mr Bailey had lived at Richmond as his main private residence during his ownership of the property.

32. There was no evidence that the local authority, bank or other financial services had been notified of the change of address.

33. Mr Bailey had lived at Tatchbrook throughout.

34. Mr Bailey did not make an election that Richmond was to be treated as his main residence under section 222(5) TCGA on the basis he had two residences.

35. There is no documentary evidence to demonstrate that it was Mr Bailey's intention to set up his main home at the property. The move to the property was for a brief duration before he returned to his original address (Tatchbrook). The agent said he only stayed at the property while it was being put on the market and sold.

36. The case law emphasises that it is the quality of occupation which counts rather than the quantity.

The Law

37. The law is not in dispute.

38. Section 222(1)(a) TCGA provides relief in respect of gains "*attributable to the disposal of…(a) a dwelling house …which is, or has at any time in his period of ownership been, his only or main residence…*".

39. Once a property has "at any time" been the individual's main residence, the relief is engaged.

40. Section 223 TCGA deals with the amount of the relief. In the form in force at the time, it provided that "*No part of a gain to which section 222 applies shall be a chargeable gain if the dwelling house…has been the individual's only or main residence throughout the period of ownership, or throughout the period of ownership except for all or any part of the last 36 months of that period.*".

41. Mr Bailey had owned Richmond for fewer than three years, so that if he had occupied Richmond at any time as his "residence" for the purposes of the Act, no CGT would be due on his disposal of it.

Discussion

42. I have found that Mr Bailey occupied Richmond on two occasions for short periods, a matter of two or three months in each case.The house was originally acquired to be a family home in 2008 and was again intended to be a home for the family when Mr Bailey moved back in 2010. He emphasised how much

better for the family Richmond was than Tatchbrook where they had been living. On each occasion, his intentions were thwarted, in 2008 by the financial crash and in 2010 by his health.

43. Mrs Sanu correctly identified that it is the quality rather than quantity of occupation which counts and there is no minimum period of residence for the relief to apply.

44. In the Court of Appeal case of *Goodwin v Curtis [1998] STC 475*, the appellant had occupied the property in question for a period of about five weeks. The Court accepted HMRC's contention that in order to turn mere occupation into "residence" for the purposes of the relief, there must be "*some assumption of permanence, continuity, some expectation of continuity"*. In that case, the appellant did not intend to live in the property permanently when he move into it. The important questions were as to the nature, quality, length and circumstances of the occupation.

45. In the First Tier Tribunal case of *Alison Clarke v HMRC[2014] UKFTT 949 (TC)* the Tribunal found that the Appellant had not discharged the burden of proof of showing that she occupied the property as her sole or main residence. The Tribunal said:

"Having weighed the evidence before us carefully, we find that the Appellant has not satisfied us on the balance of probabilities that she occupied the properties at Wandsworth Road and Ravensdene Crescent as her sole or main residence during her period of ownership. We find that the weight of evidence supports HMRC's view that she continued to occupy her flat as her main residence, and had purchased the properties as investments to be refurbished and sold on at a profit. In particular, we note that each property was owned for a short period and sold almost as soon as the refurbishments were completed. The refurbishments were extensive, which would have made it difficult to live in the properties while the works were being carried out. The bridging and other short-term loan finance arrangements on which the Appellant relied suggests to us that a short period of ownership was intended, and the Appellant was unable to support with evidence her recollection that these loans would have been converted into mortgages or state what the terms of such mortgage facilities would have been. As we understand that the Appellant did not work at the relevant time, it was not clear how she intended to make mortgage repayments in any event.

26. We also take into account the fact that the Appellant continued to use her flat as her postal address, the address at which her car was registered, and that the invoices for the refurbishment works were sent to the flat. We note that the Appellant did not register for domestic rates at the houses and that she has not produced continuous utility bills for her stated period of occupation. We note that she did not insure the properties at which she says she lived.

27. We take the view that whilst none of these factors is determinative in its own right, each piece of the jigsaw contributes to an overall picture of the Appellant's circumstances at the relevant time."

46. These circumstances were very different to those in the present case.

47. Mrs Sanu referred to other First Tier Tribunal cases which followed *Goodwin v Curtis* and emphasised the importance of "quality over quantity" when it came to occupation.

48. As noted above, I was provided with little or no documentary evidence as to the nature of Mr Bailey's undoubted occupation of Richmond. The case therefore turns mainly on his oral evidence. HMRC did not have a witness statement in advance but was content to allow Mr Bailey to give evidence and, despite having the opportunity to cross-examine, did not do so.

49. As also noted, I found Mr Bailey a straightforward witness and his evidence credible.

50. It is clear that when Mr Bailey moved into Richmond in 2008 it was intended to be a family home for him and his children and Ms Read and her son. Although a limited amount of furniture was moved in at the time, there was a reason for that. After a few months in the property, he was forced to move out due to circumstances beyond his control. It was a choice between letting the property and losing it altogether.

51. Mr Bailey did not give up on Richmond. He let it to a friend and after the friend died, he moved back, intending to move his family in when it had been decorated and painted. He rapidly found that, owing to his mental state, he was unable to cope with living in the property and decided to sell it. It is unclear how this second period of occupation fitted in with the buy-to-let mortgage which, presumably, still existed, but this does not affect my findings.

52. Taking all the circumstances into account, I am satisfied that one each occasion when Mr Bailey moved into Richmond, he intended that his residence would be on a permanent basis and that the property would be his home. I note that in 2008, the property was initially owned by Landseers Limited and I infer that when Mr Bailey acquired the property with his buy-to-let mortgage, he had to move out, so he may not have owned the property during his period of occupation in 2008. If that is so, that period of residence would not qualify him for the relief. He did own the property in the period from May to August 2010. Although his second period of occupation of the property was brief, and the period when it was occupied as his home, before he decided to sell, was even briefer, in my view, this is a case where "quality" trumps "quantity". I find that at least part of his residence in 2010 had the requisite degree of "permanence, continuity or expectation of continuity" for Richmond to have been his "residence" for the purposes of section 222 TCGA even though it was for a short time only.

53. Mr Bailey is therefore entitled to main residence relief in relation to the whole of his gain under section 223 TCGA so that no CGT is due. As the penalty under Schedule 24 Finance Act 2007 is calculated by reference to the tax due, that must also fall away.

Were the assessments in any event valid?

54. Although I have found for the Appellant on the substantive appeal, I must address further the procedural issues.

55. The onus of proof, to the normal civil standard of the balance of probabilities, lies on HMRC to show that the assessments have been validly raised. The onus then passes to the taxpayer to show, to the same standard, that he has been overcharged on the assessment.

56. HMRC opened their enquiry into Mr Bailey's 2010-11 return long after the one year enquiry window had closed. The closure notice mechanism for making an assessment under section 28A TMA was therefore not available. HMRC initially issued a closure notice but later realised their mistake and replaced it with a discovery assessment under section 29 TMA which is the correct procedure for assessing a taxpayer outside the enquiry window.

57. The time limits for opening an enquiry are part of the checks and balances in the self-assessment system which seeks to give HMRC a right to ensure that a taxpayer has paid the right amount of tax through the enquiry process but also provides a balance by giving the taxpayer certainty, after a period of time has elapsed, that his tax position is final and cannot be challenged.

58. HMRC cannot just make an assessment at any time once the enquiry window has closed. Section 29 sets out conditions which must be satisfied before HMRC can issue an assessment. The threshold for an assessment to be made under section 29, set out in sub-section (1) is that HMRC must "discover" that there is an insufficiency of tax, that is, as regards a taxpayer and a year of assessment that "*chargeable gains which ought to have been assessed to capital gains tax have not been assessed*". So HMRC must first prove that they have made such a discovery.

59. Section 29(3) provides that where a taxpayer has made and delivered a self-assessment tax return for the year (which Mr Bailey had done), he "*shall not be assessed under subsection (1)…unless one of the two conditions mentioned below is fulfilled*".

60. The first condition in section 29(4) is that the insufficiency of tax "*was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf*".

61. The second condition in section 29(5) is that "*at the time* [when the enquiry window closed] *the officer could not have been reasonably expected, on the*

basis of the information made available to him before that time, to be aware of the situation mentioned in sub-section (1) above."

62. In other words, HMRC can only raise a discovery assessment if they first prove that they have discovered an underpayment of tax and then prove that the taxpayer acted carelessly or deliberately or that the condition in sub-section (5) was complied with. The onus of proof is on HMRC.

63. HMRC did not put forward any evidence or argument on the point. Indeed, they did not even address the issue in their statement of case or at the hearing. HMRC cannot be said to have discharged the burden of proof that the section 29 assessment was properly made.

64. This has further implications.

65. Section 34 TMA lays down the normal time limits for making an assessment. The general rule in section 34(1) is that "*an assessment to…Capital Gains Tax may be made at any time not more than four years after the end of the year of assessment to which it relates.*" In the present case, the time limit expired on 5 April 2015. The discovery assessment was made on 26 February 2016 outside the four year time limit.

66. Section 36(1) TMA provides for an extended time limit: "*An assessment on a person in a case involving a loss of …capital gains tax brought about carelessly by the person may be made at any time not more than six years after the end of the year of assessment to which it relates.*"

67. Under section 36(1A) TMA, a 20 year time limit applies where the loss of tax is brought about "deliberately" by the person.

68. At the least, HMRC would have to show that Mr Bailey or Mr Baptiste had been "careless" if they wished to extend the time limit for assessing the alleged loss of tax to six years. The six year limit would have expired on 5 April 2017, so the discovery assessment would have been in time, on the basis of carelessness.

69. HMRC assessed the penalty on the basis of "deliberate" behaviour, but there was no evidence or argument on this either.

70. The onus is on HMRC to prove carelessness if they wish to extend the time limit for assessment. They presented no evidence or argument on the carelessness point and so have failed to discharge the burden of proof. It follows that the assessment made under section 29 TMA on 26 February 2016 was, in any event, out of time and so not validly made.

71. I considered whether to issue Directions requiring written submissions on these matters.

72. However, in view of my findings in the substantive matter, these errors do not make any difference to the outcome. I have found that, even if the assessments had been valid, no tax was due. I have therefore decided that, applying the overriding objective of the Tribunal to deal with matters fairly and justly, and in particular, bearing in mind the need to avoid unnecessary delay and costs, it is appropriate to proceed with a decision on the merits even though HMRC have not satisfied me that the assessments are valid. Should the parties wish to take the case any further, these matters would need to be addressed.

Decision

73. For the reasons set out above I have decided that Mr Bailey occupied Richmond as his "residence" at some time, albeit for a brief period, in his period of ownership and he is accordingly entitled to full main residence relief in respect of the gain realised on its sale. No CGT is therefore due.

74. As no CGT is due, the tax geared penalty under Schedule 24 Finance Act 2007 must also fall away.

75. I allow the appeal.

76. 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.

MARILYN MCKEEVER
TRIBUNAL JUDGE

RELEASE DATE: 31 AUGUST 2017