TC06348

Appeal number: TC/2017/00726

CORPORATION TAX – application for permission to appeal late: granted - application for exclusion of "without prejudice" material: withdrawn – application for reclassification of case from complex to standard: refused.

FIRST-TIER TRIBUNAL
TAX CHAMBER

OCEAN DEVELOPMENTS LTD **Appellant**

- and -

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

TRIBUNAL: JUDGE RICHARD THOMAS

Sitting in public at Taylor House, London EC1 on 8 February 2018

Mr Michael Firth of counsel, instructed by Morgan, Rose for the Appellant

Mr Brian Horton, of HMRC Solicitor's Office and Legal Services, for the Respondents

DECISION

1. This was a case management hearing to decide on three applications.

2. The first was an application by Ocean Developments Ltd ("the appellant") for permission to make its appeal against closure notices amending its corporation tax ("CT") assessments for the accounting periods ending 30 September 2001 to 2007 inclusive. At the end of the hearing I informed the parties that I would give permission and would give my reasons in writing.

3. The second was an application by the respondent ("HMRC") to exclude all without prejudice material from the proceedings. By this I took them to mean in any appeal proceedings. Such material was extensively referred to in the permission application without objection, and after I had given my decision on that Mr Horton said that HMRC were no longer pursuing this application. I will touch on this application again later.

4. The third was an application for the case to be reclassified from being a complex to a standard case. My reasons for denying this application are set out below.

Evidence

5. I had a witness statement with several bundles of exhibits from Mr Philip Bowles, a director of the appellant. Mr Bowles' statement was taken as his evidence in chief and he was cross-examined by Mr Horton. I am satisfied that Mr Bowles was a witnesses of truth and I accept his evidence.

6. I had a witness statement from Mr Derek Nimmo, an officer of HMRC and the investigator in this case. After a few questions from Mr Horton Mr Nimmo was cross-examined by Mr Firth. I am also satisfied that Mr Nimmo was a witness of truth and I accept his evidence, with one caveat which is not material to my decision.

Facts

7. I bear in mind that this is not a hearing of the appeal, at which many of the exhibits to the evidence would be relevant and extensively discussed. But I was urged by HMRC to find that the grounds of appeal are "very weak", and told by Mr Firth in his skeleton that "the appeal is unequivocally a strong one". I have therefore considered the testimony of the witnesses and the documents they referred to in their evidence as to the apparent merits and demerits of that appeal as part of my consideration of all the circumstances of the case, but without conducting the mini-trial that so many cases warn against.

8. These then are the basic facts relating to the appeals and the matters that led up to them.

The development

9. The appellant was incorporated by Mr Bowles in 1991 as a property developer. In about 1991/2 it acquired land known as the Taff Island site in Cardiff for £200,000 with a view to selling it for residential use (the use it has today).

10. Between 1993 and 1998 the old river bed was reclaimed and filled with inert material. The appellant instructed Ove Arup & Partners to investigate the feasibility of developing the site for residential use, but it became apparent that the site was seriously contaminated and that the old river bed would need to be dug out and remediated before any development could take place.

11. The remediation work started in 1998 and involved other land which was purchased in 2001/2. The quotations for contracts were in the tens of millions. The appellant decided to do the job itself, hiring Arup as project manager and engaging subcontractors. Once the work was done Arup signed a remediation certificate.

12. A sale of part of the site was negotiated with Wimpey in 2003 but on 10 June 2003 an administrative receiver was appointed over the company. Potential purchasers were wary of buying from the receiver, and eventually the receiver approached Mr Bowles asking him to sell the land. He agreed that the "tail end" of the remediation would be completed by a group company, Sea Island Holdings Ltd ("Sea Island").

13. In March 2004 Mr Bowles concluded a sale with Wimpey for £7.5m (including VAT) with a retention of £500,000 for the remaining remediation work. £4.2m went to the appellant's bank account (and so to the bankers who appointed the receiver) with the balance to Sea Island, as the appellant had sold the land for £4.2m to Sea Island, but the whole of the money in fact went to the bank.

Accounting and administration issues

14. Until mid-2000 the accounts were dealt with at the Heathrow offices of the group. In 2000 the appellant's accounting functions were moved to rented portacabins on the Cardiff site, but that was not a success and the appellant got behind in its accounts and returns.

15. In March 2002 a cargo airline in the group went into administration. The administrators sacked the group FD and exercised a high degree of control over the group as a whole as there were many cross-guarantees.

16. When the administration of the appellant came to an end following the sale, the administrator wished to shut down the Cardiff site. When the site manager asked what to do with contents of the portacabins he was told to get rid of them. The records destroyed included the appellant's accounting records.

Returns and dealings with the Revenue

17. Mr Bowles had been unaware the records had been destroyed and made efforts to obtain records from the receiver and got some back but not those relating to Cardiff. He asked a local firm of accountants, Lawfords, to help bring the affairs of the company up to date.

18. In or about 2008 Mr Bowles was charged with VAT fraud in relation to the sale of the site to Wimpey. He was convicted and sentenced in 2009, but before that he had contacted HMRC to ask to submit late returns because they had lost the records. He was told that they had a prima facie reasonable excuse.

19. In April 2011 when he was released from prison he contacted Lawfords and asked them to prepare the accounts from 2000 onwards. There were no accounting records as they had been destroyed nor any bank statements as more than 6 years had passed. The accounts and calculations of the remediation costs were calculated on the basis of estimated figures given by English Partnerships ("EP"), formerly the National Regeneration Agency, a government specialist adviser on brownfield sites. It was Mr Bowles' understanding that EP's published guidance is used by HMRC to check land remediation relief ("LRR") claims.

20. In the risk category that the land fell, EP's estimates were between £123k and £577k per acre, and Arup estimated £350k per acre on the basis the site was at the upper end, and those figures were used in the accounts and tax returns. The total expenditure on land remediation for 2000-2003 was estimated at £8 million.

21. The aggregate results of the accounts for 1999 to 2004 were Turnover £21.0 m, Cost of Sales £14.7m, Gross profit £6.3m, a margin of 30%. For tax purposes the costs of land remediation were multiplied by 50% to give the relief in accordance with the LRR legislation.

22. Mr Bowles acknowledged that his conviction was upheld by the Court of Appeal Criminal Division on the basis that there was not sufficient evidence of Ocean Developments incurring input VAT. I have read the decision of that court, *Bowles v R* [2010] EWCA Crim 1460 (Moses LJ, Henriques J and HHJ Roberts QC).

23. In December 2012 following submission of the accounts there was a meeting with HMRC, attended by him, Sarah Harrison ("SH"), Mr Bowles' PA and director of the company, and his accountant Mr Woolford. Lesley Hilton of HMRC is recorded in the notes of the meeting as threatening criminal prosecution of SH if she did not withdraw the LRR claim, also mentioning undisclosed income.

24. There was then protracted dialogue between the appellant and HMRC with the company refusing to withdraw the claim. On 22 April 2015 Mr Nimmo, who had taken over from Ms Hilton, wrote to the appellant.

25. In this letter he said that having reviewed information supplied in November 2014 and considered fully the circumstances of the case, and in particular the LRR claims

> "it is my intention to refer these returns for consideration by my colleagues in the Criminal Investigation directorate of HMRC. I am referring the matter to them for consideration on the basis of their previous involvement with these matters."

26. On 28 April 2015 SH wrote to Mr Nimmo withdrawing the "late" claims to LRR contained in the returns for the 8 years to 30 September 2007.

27. In a letter of 29 May 2015 headed "Without Prejudice" Mr Nimmo wrote to Lawfords. Relevant passages are:

> "HMRC has consistently outlined their concerns regarding the validity of the claims [to LRR] and generally the accuracy of the figures contained within the returns submitted, and on the basis of the earlier criminal proceedings, offered the current director [SH] the opportunity

> on a without prejudice basis to withdraw the Self Assessment returns, when they met on 19 December 2012.
>
> Subsequent offers to withdraw the accounts, returns, claims to losses and [LRR] were made, but these were conditional and not acceptable to HMRC.
>
> Whilst correspondence continued, the wording of subsequent communications reverted to discussing withdrawal of [LRR], which had been the main area of concern, as opposed to the withdrawal of the returns/accounts which in effect contained the claim to losses and [LRR] …
>
> On the basis of what [SH] has set out in her letter, there is no problem in withdrawing those claims to [LRR], but if that is all that is withdrawn, the remainder of the entries in the … returns … remain in place and will need to be actioned. The result of such actions is that circa £8.7m of profits become chargeable to [CT]. … there are clearly concerns about what the true level of profits or losses should be.
>
> … there is no evidence that the company has funds or assets.
>
> With a view to bringing this matter to a conclusion there are as I see it 2 options, the first being that [SH] unconditionally formally withdraws the [returns] …. The second option, based on withdrawal of the [LRR] claim (as she has done) is that on the basis of the lack of evidence to support the returns submitted for all years, and taking account of the overall history of this case that on a Without Prejudice basis a No Profit/No Loss position is agreed…"

28. SH resigned on 30 September 2015 and Mr Bowles became a director again in December 2015.

29. On 7 September 2016 Mr Nimmo issued closure notices and amendments of returns for the years concerned. It seems that on each of the notices of the amended figures Mr Nimmo wrote

> "Based on CT return excluding the land remediation relief which has been withdrawn following letter of 28 April 2015"

30. Mr Bowles maintained that they were sent to Lawfords but not to the appellant.

31. In late October 2016 the appellant received warning of winding up proceedings unless £3.5 million was paid.

32. Lawfords were not at that time providing any help to the appellant because of a dispute over fees. On 7 September 2016 Mr Woolford sent the notices he had received to Mr Bowles.

33. At a meeting in October 2016 Mr Bowles says he was told by Mr Woolford that as the debt was based on the appellant's own returns the notices could not be appealed. Mr Bowles thought that the winding up threat was simply a mistake.

34. When he received the petition for winding up Mr Bowles saw that it said that the demand was "in accordance with the company tax returns made by the company", but neither Mr Bowles nor his solicitors Morgan Rose had seen the returns.

35. On 10 January 2016 Mr Woolford provided the returns to Morgan Rose. When they realised that the tax debts were not based on the returns as submitted they lodged appeals the next day with a request that they be admitted late under s 49 Taxes Management Act 1970.

36. On 13 January 2017 the appeal (as Mr Bowles describes it) was formally notified to the Tribunal. On 15 May 2017 the Companies Court rejected the winding up petition, as HMRC had failed to file any evidence. HMRC were relieved from sanctions.

Submissions on the late appeal issue

37. Mr Firth for the appellant had a preliminary issue about jurisdiction. It was his contention that there were no valid closure notices issued, and so there was nothing against which the appellant could make a valid appeal, and therefore nothing which could be determined by the Tribunal.

38. To make that point good he submitted that the closure notices were invalid because

(1) the purported closure notices did not state Mr Nimmo's actual conclusions

(2) they did not directly state *any* conclusions.

39. A substantial part of his cross-examination of Mr Nimmo was directed to establishing these points.

40. HMRC did not make any submissions on this point.

41. If that point was not accepted, Mr Firth argued in support of the application for permission that the lateness was explicable and excusable by reference to five factors

(1) the closure notices were not received by the appellant, only his accountants who did not inform Mr Bowles about them and he was unable to get hold of them for a long time

(2) the notices do not draw attention to the right of appeal, how to make it and who to

(3) the appellant was embroiled in a dispute with his accountants over fees so did not obtain proper advice

(4) in fact the appellant was misinformed by their accountants about the correctness of the tax bill in the winding up petition, wrongly saying that it was in accordance with the returns

(5) The appellant was not told of his appeal rights by HMRC when he asked about the tax bill in the winding up petition.

42. On the issue of prejudice, Mr Firth said HMRC have not been prejudiced by the delay. HMRC waited over a year from the letter of 29 May 2015 before amending the returns and issuing large tax bills.

43. The appellant on the other hand would be extremely prejudiced if they are not allowed to appeal. Its case is a strong one, as HMRC's amendments assume an impossible position that the remediation works carried out by the appellant did not cost

anything and that a 75% margin was achieved. HMRC must know that the profits they assessed are imaginary.

44. In support of his arguments Mr Firth cited *Elazoua v HMRC* [2014] UKFTT 75 (TC) (Judge Howard Nowlan and Mr Michael Bell) at [7].

45. Mr Horton for HMRC submitted that, taking the five well known *Data Select* questions in turn

(1) the purpose of the time limit for appealing of 30 days is to ensure finality in the outcome of a tax enquiry. Matters thought by one party to be long concluded should not be resurrected after a long delay

(2) the delay was about 3 months and was significant

(3) there was no good explanation for the delay. The closure notices were issued to the address on record, the appellant was professionally advised throughout this period and the appeal rights are clear

(4) the consequences of an extension of time for HMRC are that they would incur substantial litigation costs. HMRC cite *R (oao Dinjan Hysaj) v SSHD* [2014] EWCA Civ 1633 ("*Hysaj*") for the proposition that the merits should only be considered if the Tribunal can see without much investigation that the grounds of appeal are either very strong or very weak. In this case HMRC say the grounds are very weak, as the issue of remediation costs was considered in detail by the Court of Appeal in *Bowles v R* and that court found that there was no evidence of the costs that were purportedly incurred by the appellant. Grounds of appeal relating to the availability of group relief are also very weak.

(5) as to considering "all the circumstances" as required by *Denton*, HMRC say the appellant has failed to engage with the appeal process.

Discussion

The jurisdiction point

46. After I informed the parties that on the basis of what I had read and heard I would allow the application for permission, I asked Mr Firth if he wished to press his point on jurisdiction. He said he did not and so I have come to no conclusion on the point. I will though say that I consider that Mr Nimmo had stated his conclusions. And under cross-examination Mr Nimmo said that he did not believe that the appellant had actually made the amount of profits that were reflected in the closure notices. The significance of that in legal terms is for another occasion.

Approach to the application

47. It did not come as a surprise to the Tribunal that among the cases cited by Mr Horton in his skeleton were *BPP Holdings v HMRC* [2017] UKSC 55 ("*BPP*"), *Denton v TH White Ltd (and related appeals)* [2014] EWCA Civ 906 ("*Denton*") and *Data Select Ltd v HMRC* [2012] UKUT 187 (TCC) ("*Data Select*"), as well as *Hysaj*.

48. From *BPP* I know that while the Civil Procedure Rules ("CPR") of the Courts in England and Wales do not apply to this or any other Tribunal applying the law in that jurisdiction (which we are in), we are expected to apply the same principles but having

regard to the overriding objective of the Tribunal rather than any similar statement in the CPR.

49. That means that I should follow the three stage approach in *Denton* to applications from relief from sanctions, and I know from *Hysaj* that an application to do something after the time permitted by either the Rules of the tribunal or any enactment is to be treated in the same way as an application for relief from sanctions.

50. *Data Select* is binding on this Tribunal. Although it, a decision of the Upper Tribunal, was applying a previous version of the CPR by analogy, nothing in *BPP* suggests that the five questions suggested as relevant in *Data Select* are not relevant any longer. Indeed those questions may be seen as reflected in the three stage *Denton* approach.

Denton Stage 1

51. A delay of three months by reference to an appeal period is serious and significant. The appellant did not appear to gainsay this.

Denton Stage 2

52. If it is correct that the appellant did not receive the closure notices then in my view there was good reason for the delay. It may be correct to say, as HMRC do, that the notices are deemed to have been served on the appellant by s 7 Interpretation Act 1978, but that is subject to two qualifications. First, if the appellant can prove that they did not in fact receive the notice that may nullify the s 7 presumption. Second, the question of service of the closure notices does not determine the issue, but is a factor to be taken into account in considering all the circumstances.

53. As to service it was Mr Bowles' evidence that the appellant did not receive them. The appellant's conduct after September 2016 is consistent with this evidence. Given what had happened in the lengthy and fraught discussions with HMRC I find it unlikely that Mr Bowles would have adopted a casual attitude to being landed with a tax bill in the millions when he thought that a no profit, no loss basis was HMRC's position. This apparently relaxed attitude contrasts very strongly with Mr Bowles' reaction when the demand and winding up petition arrived.

54. It is undoubtedly the case that once they realised what had happened the appellant took immediate steps to remedy the situation.

55. I also find that Mr Bowles' belief that withdrawal of the LRR claim would lead to a no profit/no loss position was well founded. The letter of 29 May 2015 from which I have quoted extensively at §27 is extremely confusing. On the one hand Mr Nimmo says that without a complete withdrawal of the returns profits of £8.7 million become chargeable but on the other he clearly says that the other option, withdrawal of LRR claim (which was done), would lead to no profit/no loss. This would have lulled Mr Bowles into a false sense of security.

Denton Stage 3

56. I do not agree with HMRC that it is apparent without much investigation that the merits of the appeals are very weak, for two reasons.

57. First, I do not think that *Bowles v R* can bear the weight HMRC put on it. On a perhaps pedantic point the appellant, as distinct from Mr Bowles, was not, so far as I can tell, charged with any offence, let alone convicted. It was not even the appellant's VAT liability that was in issue, it was Sea Island's.

58. Second I do not understand HMRC's conclusion that by the withdrawal of the LRR claim the appellant gave up any right to a deduction of the remediation costs.

59. It is necessary at this point to refer to some of the legislation for LRR, which at the time was in Schedule 22 Finance Act 2001 (it is now in Part 14 Corporation Tax Act 2009). The relevant parts of Schedule 22 are

"**PART 1 DEDUCTION FOR CAPITAL EXPENDITURE**

DEDUCTION FOR CAPITAL EXPENDITURE

1—(1) This paragraph applies if—

(a) land in the United Kingdom is, or has been, acquired by a company for the purposes of a trade carried on by the company,

(b) at the time of acquisition all or part of the land is or was in a contaminated state (see paragraph 3), and

(c) the company incurs capital expenditure which is qualifying land remediation expenditure in respect of the land (see paragraph 2).

(2) For the purposes of corporation tax such capital expenditure as is qualifying land remediation expenditure shall (if the company so elects) be allowed as a deduction in computing the profits of the trade for the accounting period in which that expenditure is incurred.

(3) For the purposes of sub-paragraph (2) any capital expenditure incurred for the purposes of a trade by a company about to carry it on shall be treated as if it had been incurred by that company on the first day on which it does carry it on and in the course of doing so.

(4) Sub-paragraph (2) shall not apply to so much of the qualifying land remediation expenditure as—

(a) represents expenditure which has been allowed as a deduction in computing the profits arising from the trade for any accounting period preceding the period in which the expenditure is incurred, or

(b) represents capital expenditure in respect of which an allowance has been, or may be, made under the enactments relating to capital allowances.

(5) A company is not entitled to a deduction under this paragraph in respect of expenditure on land all or part of which is in a contaminated state, if the land is in that state wholly or partly as a result of any thing done or omitted to be done at any time by the company or a person with a relevant connection to the company.

(6) An election under this paragraph must specify the accounting period in respect of which it is made.

(7) The election must be made by notice in writing to the Inland Revenue.

(8) The notice must be given before the end of the period of two years beginning with the end of the company's accounting period to which the election relates.

QUALIFYING LAND REMEDIATION EXPENDITURE

2—(1) For the purposes of this Schedule "qualifying land remediation expenditure" of a company means expenditure of the company that meets the conditions in sub-paragraphs (2) to (6).

(2) The first condition is that it is expenditure on land all or part of which is in a contaminated state (see paragraph 3).

(3) The second condition is that the expenditure is expenditure on relevant land remediation directly undertaken by the company or on its behalf (see paragraph 4).

(4) The third condition is that the expenditure is incurred—

(a) on employee costs (see paragraph 5), or

(b) on materials (see paragraph 6),

or is qualifying expenditure on sub-contracted land remediation (see paragraphs 9 to 11).

(5) The fourth condition is that the expenditure would not have been incurred had the land not been in a contaminated state (see paragraph 7).

(6) The fifth condition is that the expenditure is not subsidised (see paragraph 8).

…

PART 2 ENTITLEMENT TO LAND REMEDIATION RELIEF

ENTITLEMENT TO RELIEF

12—(1) This paragraph applies if—

(a) land in the United Kingdom is, or has been, acquired by a company for the purposes of a trade carried on by the company,

(b) at the time of acquisition all or part of the land is or was in a contaminated state, and

(c) the company incurs qualifying land remediation expenditure in respect of the land.

(2) A company is entitled to land remediation relief for an accounting period if the company's qualifying land remediation expenditure is deductible in that period.

(3) The company's qualifying land remediation expenditure is deductible in that period if it is allowable as a deduction in computing for tax purposes the profits for that period of a trade carried on by the company.

(4) A company is not entitled to land remediation relief in respect of expenditure on land all or part of which is in a contaminated state, if the land is in that state wholly or partly as a result of any thing done or omitted to be done at any time by the company or a person with a relevant connection to the company.

PART 3 MANNER OF GIVING EFFECT TO RELIEF

> **13** Where—
>
> (a) a company is entitled to land remediation relief for an accounting period,
>
> (b) it is carrying on a trade in that period, and
>
> (c) it has qualifying land remediation expenditure that is allowable as a deduction in computing for tax purposes the profits of … the trade for that period,
>
> it may (on making a claim) treat that qualifying land remediation expenditure as if it were an amount equal to 150% of the actual amount."

60. I do not have the materials to be able to say why HMRC sought so strenuously to get the appellant to withdraw its LRR claim, but withdraw it it did. What was the effect in law of that withdrawal?

61. To find this I think it is useful to look at the accounts and CT return of the appellant for one period, for which purpose I look at the accounting period ended 30 September 2003.

62. The accounts show

Sales	£2,100,000
Remediation costs	£897,914
Net profit before taxation	£826,895

Notes show "No liability to UK CT arose"

63. The CT return (CT600 (2008) version) shows "This return contains estimated figures" and

Turnover	£2,100,000
Trading profits	£543,187
Land remediation enhanced expenditure (Enter 150% of actual expenditure)	£1,350,373

64. The land remediation amount represents 150% of £900,248, £2,334 more than the accounts figure.

65. Where the profits of a trade are calculated for the purposes of CT, the starting point is a set of accounts drawn up in accordance with GAAP (s 42 FA 1998). The accounts say they were prepared under the FRSSE (part of UK GAAP). LRR provides two separate departures from GAAP: paragraph 1 allows for an election to treat qualifying land remediation expenditure (as defined in paragraph 2 ("QLRE")) which is capital expenditure as deductible in the year it was incurred. Paragraph 12 gives a relief (LRR) for all QLRE which is deductible in a year. The claimant may claim to treat the QLRE as if it were 150% of the actual amount.

66. It seems to me that it is strongly arguable that the effect of withdrawal of a claim for LRR is that the amount of QLRE that may be deducted is 100% of the amount, and

not 150%, so that the taxable gross profit in 2003 is the same as the accounting profit, subject to other tax adjustments.

67. The tax shown on the closure notice for this period was £567,367.50. The CT rate for both financial years involved was 30% so the trading profits that this rate assumes are £1,891,223. It must follow that Mr Nimmo, as he said he did, excluded all the QLRE, not just the enhanced amount.

68. I do not say that all the amount treated as QLRE by the appellant is deductible. I do not have the materials to tell, and in any case that would be doing "much investigation" which *Hysaj* says I shouldn't. What I can say without much investigation is that it seems to me unlikely in the extreme that in an appeal the appellant would not be able to establish a deduction for any land remediation expenditure at all.

69. It is not sufficient for HMRC to say – "look at the criminal case". Mr Bowles sought to explain why what is said there should not be taken to be determinative of any claim to deduct remediation expenditure. Again I do not know if the appellant will, or to what extent, succeed on any appeal. That is not my concern. What I say is that HMRC are wrong to say that there is a very weak case for overturning the amendments made by Mr Nimmo to the appellant's self-assessments.

70. As to group relief claims I am not in a position to comment save to note the possibility (than which I put it no higher) that paragraphs 61 to 64 Schedule 18 FA 1998 might be relevant.

71. I agree therefore with Mr Firth that the prejudice to the appellant is not just that it will have to pay the tax or more likely be wound up, with what if any repercussions on the directors I do not know, but the real prejudice is that the tax on the basis of which HMRC has sought and may in future seek to wind up the appellant is strongly arguable to be to a substantial extent, if not entirely, illusory. Mr Nimmo seemed to agree.

72. Taking all the circumstances into account, including the prejudice to both parties if the decision goes against them, the not exorbitant delay and the reasons for the delay, and (without much investigation) the merits, I grant permission to appeal to HMRC.

73. I leave HMRC to ponder on wise words of one of the greatest judges in history, Judge Learned Hand of the US Second Circuit Court of Appeals. In *George M Cohan v Commissioner of Internal Revenue* (1930) 39 F2d 540, Judge Hand said

> In the production of his plays Cohan was obliged to be free-handed in entertaining actors, employees, and, as he naively adds dramatic critics. He had also to travel much, at times with his attorney. These expenses amounted to substantial sums, but he kept no account and probably could not have done so. At the trial before the Board he estimated that he had spent eleven thousand dollars in this fashion during the first six months of 1921, twenty-two thousand dollars, between July first, 1921 and June thirtieth, 1922, and as much for his following fiscal year, fifty-five thousand dollars in all. The Board refused to allow him any part of this, on the ground that it was impossible to tell how much he had in fact spent, in the absence of any items or details. The question is how far this refusal is justified, in view of the finding that he had spent much and that the sums were allowable expenses. Absolute certainty in such

> matters is usually impossible and is not necessary; the Board should make as close an approximation as it can, bearing heavily if it chooses upon the taxpayer whose inexactitude is of his own making. But to allow nothing at all appears to us inconsistent with saying that something was spent. True, we do not know how many trips Cohan made, nor how large his entertainments were; yet there was obviously some basis for computation, if necessary by drawing upon the Board's personal estimates of the minimum of such expenses. The amount may be trivial and unsatisfactory, but there was basis for some allowance, and it was wrong to refuse any, even though it were the travelling expenses of a single trip. It is not fatal that the result will inevitably be speculative; many important decisions must be such. We think that the Board was in error as to this and must reconsider the evidence.

The "without prejudice" material

74. Mr Horton withdrew his objection to the material. I think he was right to do so.

Reclassification

75. Mr Horton did not withdraw his application for reclassification. He was prepared to take my jibe that seeking to reduce the classification to standard could be viewed as an attempt to avoid paying costs in the likely event of a defeat. His argument was that looking at the "gateways" in Rule 23(4) of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (SI 2009/272, only sub-paragraph (c) was passed through in this case, as he accepted the amount of tax was a large sum.

76. He submitted that the case on appeal would take 2 to 3 days and that was not long, and he said that the question whether the appellant has the evidence to support the expenditure is not a complex or important principle or issue.

77. In my view 2 to 3 days is very likely to be an underestimate. This application took the whole morning going into the usual time for the short adjournment, and was fairly truncated with issues dropped rather than being argued.

78. There were well over 1,000 pages of documents in the three bundles making up the exhibits to Mr Bowles' evidence in this application. In the absence of any documents and records of many contemporary matters, oral evidence of what happened is likely to be crucial (and lengthy).

79. As to principles it seems to me to be an important issue to consider to what extent it is possible to use circumstantial evidence to support entries in accounts and tax computations when the contemporary records have been inadvertently destroyed or are no longer available. And it may be necessary to consider the LRR legislation in depth, something which has so far as I can tell featured in only one previous decision of this Tribunal, *Dean & Reddyhoff Ltd v HMRC* [2013] UKFTT 367 (TC).

80. HMRC are of course entitled to revisit this issue, but case management has not yet started and it would in my view be best to see how matters progress before any application is renewed.

81. 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: 20 FEBRUARY 2018