TC01644

Reference no: TC/2010/06899

Income Tax - National Insurance Contributions - Value Added Tax - whether Mrs. Valantine was in partnership with her husband, and thus liable as partner for her share of the partnership income tax liabilities and for the whole of the VAT liability of the business, clearly conducted by her husband - Appeal allowed

FIRST-TIER TRIBUNAL

TAX

MRS. PAULINE VALANTINE

Appellant

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Tribunal: HOWARD M. NOWLAN (Tribunal Judge)
CAROLINE DE ALBUQUERQUE

Sitting in public at 45 Bedford Square, London, on 17 August 2011

Graham Eldred of Ravensbourne Business Centre on behalf of the Appellant
Sue Spencer of HMRC's Criminal Investigation service on behalf of the Respondents

DECISION

Introduction

1. This was a simple but rather sad case. It was ADMITTED that the Appellant's husband ("Mr. Valantine") had been trading as a landscape gardener from approximately April 2004 until the business ceased in April 2008, and that Mr. Valantine had failed to make any returns for the purposes of Income Tax, Class IV National Insurance Contribution or VAT to HMRC. It was, however, equally clear that Mr. Valantine was unable to pay any of the liabilities, as he was about to declare himself bankrupt. He had indeed initially sought advice from Mr. Eldred, who was representing the Appellant in this case, and Mr. Eldred had confirmed that Mr. Valantine had no defence to the various assessments made against him, but that equally he was obviously unable to pay the liabilities and would indeed have to declare himself bankrupt.

2. On various grounds that we will mention below, HMRC considered that Mr. Valantine's trade had been a partnership trade with his wife. Whilst one consequence of this was that the aggregate liability to income tax would have been reduced (because each partner would have been entitled to their personal reliefs and less of the profit would have attracted tax at 40%), the material consequence of the partnership contention was that the Appellant received assessments for her share of the partnership profits for Income Tax and Class IV NIC purposes, and potentially being jointly liable for the VAT, she was assessed for the whole of the alleged partnership's VAT liability. She did have some assets, and were the assessments upheld, there would have been every prospect of HMRC recovering the tax assessed on the Appellant.

3. The case thus depended entirely on whether the Appellant was indeed carrying on the landscape gardening trade in partnership with Mr. Valantine. We concluded with no hesitation that she was not. The case had in fact been well prepared by HMRC, and Mrs. Sarah Baynes, the relevant case officer who gave evidence before us, had prepared the case both carefully, and with some compassion, and we consider that HMRC are to be commended, and not criticised, for the way in which they handled and presented the case. Nevertheless, during the hearing it is fair to say that, first, much of the evidence on which the partnership contention had been based collapsed and, more significantly, our understanding of the personal circumstances obtaining between Mr. Valantine and the Appellant made it unthinkable that the Appellant had been a partner in the relevant business. Accordingly the various appeals are all allowed.

The facts in more detail

4. The Appellant and Mr. Valantine had been in partnership as landscape gardeners for many years when they lived in London, the partnership name then being Valantine Wilkins. The Appellant's father had presumably started the business, Wilkins being the Appellant's maiden name and, when they were trading in London, their two sons assisted in the business.

5. As we understood matters, the Appellant was then actively engaged in the business, contributing to the work, and also attending to the bookkeeping, accounts and tax affairs. We believe that there were no irregularities in the returns for tax purposes in those days.

6. On account of Mr. Valantine's serial infidelity, the marriage broke down in about 1999, and at one point the Appellant sued for divorce. The divorce petition was turned down for lack of evidence in that the application had been on the grounds of separation, whilst in fact Mr. Valantine and the Appellant were still living, though separately, in the same house. The Appellant did not pursue the divorce petition and it was not until September 2002 that the partnership business of Valantine Wilkins formally ceased. Also in September 2002, their jointly-owned house, referred to as "the Geraldine Road property" was sold for £291,000. Following the repayment of two mortgages of a figure somewhat in excess of £30,000, Mr. Valantine agreed informally that the Appellant could keep the net proceeds, he retaining simply a Range Rover, and the Appellant then bought a property in Vale Road, also in London, in her sole name for £231,000. Mr. Valantine apparently went to Europe.

7. In July 2003, Mr. Valantine returned to the UK and persuaded the Appellant to give the marriage "a further go", albeit subject to a number of conditions, on which she insisted. It was perfectly clear to us during the hearing that the Appellant was a fairly strong character and that she was unwilling to trust Mr. Valantine wholeheartedly ever again. She thus insisted that if they were to live (still separately but) under the same roof, they would have to move well away from London and therefore the Appellant sold the Vale Road property at a profit of £40,000, and bought a house, Beech House, in Yorkshire, again in her sole name. The surpluses that she had available from these various property transactions amounted to about £50,000 which she credited to her Halifax bank account.

8. In about September 2003, Mr. Valantine joined his wife at Beech House and sought to start his own landscape gardening business under the name "Muddy Wellies". At that time, Mr. Valantine had no bank account, and had been unable to obtain a bank account, and so whilst she adamantly insisted that she was not prepared to be engaged in any way in the business, the Appellant accepted that she was prepared to assist Mr. Valantine in setting up the business in various ways.

9. One significant element of assistance was that the Appellant bought a second-hand Land Rover which, owing to defects,had to be swapped for a second-hand Range Rover, and she also bought a VW Golf van. Both were registered in her name, but she made them available for use by Mr. Valantine, a tow-bar being fitted to the Range Rover so that it could pull a trailer and equipment. The deal appeared to be that, whilst the Appellant would retain "control" or "security" over the vehicles in the respect that they were registered in her name, Mr. Valantine would gradually reimburse her, or pay her for the use of the vehicles out of the takings of the business.

10. The Appellant assisted in other ways. Since she alone had a bank account until Mr. Valantine managed to secure an HSBC account in February 2004, the Appellant made the arrangements for an advertisement to be inserted into at least one local paper, and paid for the advertisement with her own cheque. She dealt in a similar manner with opening a business account at a local garden centre, though we understood that goods were in fact only purchased on one occasion from this garden centre.

11. There was no dispute about the fact that the Muddy Wellies business was conducted from about September 2003 until some time in the tax year ended 5 April 2008. During this period reasonable profits were made but Mr. Valantine never made a return for Income Tax, National Insurance or VAT purposes, and when he paid workers, he never deducted PAYE tax or National Insurance contributions from the amounts paid to employees. Mr. Valantine said that he had been under considerable

stress during this period and that, whilst he knew that he should have made the returns for the various tax purposes, he frankly "never got round to it". When the Appellant was asked whether she knew that the returns had not been made, she said that she had reminded Mr. Valantine on several occasions that he should get up to date with his paperwork, but she had eventually been told simply to "mind her own business", and that "he had it in hand".

12. It was not until some police investigation in relation to different matters in 2009 that Mr. Valantine's papers were removed from the house, and in due course sent to HMRC. The papers were far from complete. They included all estimates that had been sent by Mr. Valantine for proposed work, various purchase invoices and bank statements and paying-in books, but no sales invoices or diary entries indicating work actually undertaken.

13. In 2010 HMRC opened an enquiry into Mr. Valantine's tax affairs. With a view to trying to estimate turnover and profit, they took a sample of approximately 140 estimates that had been sent out by Mr. Valantine (possibly out of over a thousand estimates), and wrote to the customers or potential customers, asking various questions in an effort to establish the level of trading, turnover and profits.

14. The tax enquiry resulted in VAT assessments for some periods, but not for those where the estimated turnover fell below the registration thresholds prevailing from time to time. HMRC pointed out that the total amount of Income Tax being assessed on both Mr. Valantine and the Appellant (once it was contended that the two were in partnership) was less than it would have been had the entire estimated profits been assessed just in the name of Mr. Valantine. Whilst nothing turned on this, we actually assume that the true taxable profits were considerably less than the estimated figures because no deduction had been given for payments to workers because Mr. Valantine had refused to reveal the names and details of the people who had obviously worked for the business.

15. It appeared to be accepted that whatever amounts were assessed on Mr. Valantine, nothing or very little would be paid because he would petition for bankruptcy. This was of no concern to us because the sole issue for us was whether the Appellant was in partnership in the Muddy Wellies business with Mr. Valantine.

The contentions advanced on behalf of the Respondents

16. It appears fair to summarise HMRC's case as being founded essentially on three arguments, the points in the second and third bullet points below being of essentially the same nature. They were that:

- since the Appellant had been an acknowledged partner in the earlier business of Valantine Wilkins, it seemed entirely natural that she would be a partner in the Muddy Wellies business;
- whilst the enquiry letters sent out to the recipients of the sample estimates had been designed to establish turnover and profits of the business and not to ascertain whether the Appellant had been a partner, two at least of the responses received indicated that the Appellant had done some work in relation to a pond for one of the customers, and she had collected moneys owing from another customer, these two responses suggesting that the Appellant was involved in the business;
- in the same vein as the point just made, the feature of the Appellant paying for advertising for the business, and opening an account at the garden centre again suggested that she was involved in the business. In particular, even the advertisement referred to the business as being "a family business"; and
- most significant of all, some of the business customers had paid their accounts (in whole or in part) by cheque directly into the Appellant's bank account. Giving the rough figures for the tax years ending on 5 April 2004 to 5 April 2008, customer cheques in the rough amounts of £18,000, £22,000, £7,000, £6,000 and £5,000 had been paid into the Appellant's bank account. In addition Mr. Valantine had made various transfers from his account to the Appellant's account, of the aggregate amount of about £7,500. Accordingly it appeared that approximately £64,500 had been credited to the Appellant's bank account either in the form of cheques from customers of the Muddy Wellies business, or by way of the transfers just mentioned.

The evidence and the contentions on behalf of the Appellant

17. Both Mr.Valantine and the Appellant gave evidence, and their evidence seemed entirely straightforward and honest. The honesty of the Appellant's evidence extended not only to the minor detail points addressed, but also to her very firm attitude in relation to the limited (and still largely separate) relations that she had with Mr. Valantine.

18. We will deal with the less important minor points first. In relation to them, it seems fair to say that insofar as HMRC's case was based on these points, it somewhat foundered.

19. We accept that many wives, even semi-estranged wives, will support the work and activities of their husbands in minor ways without that occasioning any serious contention that the two are in partnership. HMRC conceded this point as a generality, though their contention had been that the few examples of support and work that they had produced were part of a wider picture.

20. We were told that the occasion where one person replying to the 140 circular letters had referred to the Appellant assisting in relation to a pond was some very limited help in putting some lilies into the pond, when Mr. Valantine was in the pond actually then taking and inserting the lilies into the pond. The occasion where the Appellant had collected amounts owing to Muddy Wellies resulted from the fact that

Mr. Valantine had been arrested in relation to charges that were in due course dropped, and he had asked the Appellant to collect moneys owing in order that he could pay the workers who had been involved with the particular project. We accepted that the accounts by Mr. Valantine and the Appellant of the very minor involvement being given by the Appellant were far more consistent with the feature of minor elements of assistance being given on an informal basis, and we accepted that they provided no evidence of the Appellant being in partnership with Mr. Valantine.

21. Another example advanced by HMRC was of a design being sent with one of Mr. Valantine's estimates, and the suggestion that it was the Appellant who had undertaken design work in the Valantine Wilkins partnership, so that it seemed reasonable to suppose that she was responsible for design work undertaken in the Muddy Wellies partnership.

22. We accept the Appellant's evidence that she had never done the design work even in the Valantine Wilkins partnership. It was apparently one of the couple's sons who had periodically sketched designs for clients in the former Valantine Wilkins partnership. Moreover the design plan that accompanied the estimate, on which HMRC were basing their contention, was in fact the client's own plan, sent to Mr. Valantine so that he could judge accurately what was required to be done when submitting his estimate. It was not a design that had been prepared by anyone on behalf of Muddy Wellies at all.

23. We also accepted that references in adverts to the business being "a family business" were explained by the fact that for many years Mr. Valantine had been used to referring to the business in this way, particularly because the couple's sons had been involved with the business when it was undertaken in London. We even understood that on at least one occasion one of the sons helped with the work in Yorkshire. Accordingly we felt unable to base any serious conclusion on the proposition that the phrasing of the advertisement indicated that the Appellant was a partner.

24. The Appellant's contention in relation to why customers of Muddy Wellies had sometimes paid their invoices to the Appellant, rather than to Mr. Valantine, and the explanation as to why various account transfers, totalling about £7,500, had been made from Mr. Valantine to the Appellant was that Mr. Valantine was thereby reimbursing the Appellant for the cost of purchase of the Range Rover and the VW Golf van, and the costs of insurance and licensing the two vehicles, and thereafter he was reimbursing her for his share of living expenses. These expenses included food, a share of the household utilities, much the greater part of the phone bill, and other similar items. It was conceded that no accurate calculation had been made of how much Mr. Valantine owed in respect of these items, and neither the Appellant nor Mr. Valantine knew whether the payments had fully reimbursed the Appellant for the various costs of the vehicles.

25. We might add, though no point was made in relation to this at the hearing, that the ratio in which amounts were credited to Mr. Valantine's account (once it was opened) and the Appellant's account bore no particular relationship to each other, period by period, save that in the last two relevant years, the payments into the Appellant's account were in the fairly modest amount of roughly £5,000. The ratio of the payments to the two accounts fluctuated widely in all periods. In all years, the amounts credited to Mr. Valantine's account had been very considerably greater (roughly 5 times the amounts credited to the Appellant's account in aggregate, even when adding in the £7,500). Were one meant to suppose that the two were in partnership and that the profit-sharing ratio would have been governed by the split in

the allocation of payments between the two accounts, the conclusions would have had to be drawn that the profit-sharing ratios were constantly changing, and that the profit-sharing split was nowhere near 50/50.

26. Evidence was also given in relation to the relationship between Mr. Valantine and the Appellant, and the Appellant's general attitude to not trusting her husband, being prepared or not to join him in a partnership venture, and wishing to retain control over what had become "her assets" just in case there should be a further deterioration in the relationship.

27. We will summarise this element of the evidence only in very general terms. We both independently gained the impression that Mr. Valantine's past unfaithfulness had irretrievably undermined the relationship between Mr. Valantine and the Appellant. Mr. Valantine conceded this, and apologised for it, and explained that this was why, when their original house had been sold, he had informally allowed his wife to take virtually the totality of the joint assets, even though the original house had been jointly owned.

28. For her part, it was absolutely clear to us that the Appellant mistrusted Mr. Valantine in several respects, perhaps the least significant being his dealing with money. It was clear to us that even though they might live under the same roof, they were unlikely to live again as a normal couple. It was equally clear that, having obtained some security by becoming the sole owner of the house, and by owning the bulk of the cash, when the Appellant bought the Yorkshire house, her attitude was that even if she was prepared to pay for the vehicles, she would be and remain the registered owner of the vehicles, so that if they had to be sold on a further break-up, she would retain the proceeds. We believed the Appellant when she said that she would never contemplate being in partnership with her husband, either in a business or in various other respects. They appeared to live together, largely out of necessity, and the lack of trust shown by the Appellant was manifest.

Our decision

29. We had no doubt that the Appellant was not jointly engaged in a partnership business with her husband. The business was clearly his business, albeit that in some ways she had financed some items. She was not only not actually actively engaged in the trading; she manifestly had nothing to do with the running or the management of the business; and whilst she received some cash, funded out of the profits that Mr. Valantine made, those receipts were far more realistically attributed to the reimbursement of the major items that she had paid for, and to her insistence that he should pay for his share of the living expenses, than to any notion that they were jointly sharing in the partnership profits.

30. Virtually all of the detailed points on which HMRC had relied in advancing their case had been shown to be of minor, or no, significance in relation to the partnership contention. We might additionally note that not only did HMRC not produce the responses (where there were either written or phone responses to the 140 letters that they sent to customers and potential customers), other than the two that we have referred to above, but if only two people of those replying to the survey made any reference that had any bearing on whether the Appellant was engaged in the business in any way, and those two references have been explained, it seems more realistic to conclude that the survey undermined, rather than supported, the partnership contention.

31. The fundamental point, however, is that the estranged relations between Mr. Valantine and the Appellant made it unthinkable to us that the Appellant would have engaged in any way in the business that we believe that Mr. Valantine was running as a sole trader.

32. In allowing the appeal, and rejecting HMRC's contentions fairly firmly, we repeat the remarks made in the Introduction that we do not suggest that the case officer should be criticised in any way. HMRC's case was assembled very carefully and properly, and the case officer appeared to have acted reasonably throughout. We feel that the case might not have been pursued to an appeal if Mr. Valantine and the Appellant had been prepared to discuss matters at a meeting with HMRC. As it was, the somewhat rough approach on the part of Mr. Valantine, and the statement by the Appellant that she was not prepared to enter into discussions with anyone who suggested that she was prepared to enter into a partnership business with Mr. Valantine probably accounted, at least in part, for why this case had ultimately involved litigation.

Right of Appeal

33. This document contains full findings of fact and the reasons for our 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.

HOWARD M. NOWLAN (Tribunal Judge)

Released: 9 December 2011