UK Tax Bulletin

November 2018

Field Court Tax Chambers

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Latest Rates of Inflation and Interest

The following are the current rates at November 2018

Current Rates	
Retail Price Index: September 2018	284.1
October 2018	284.5
Inflation Rate: September 2018	3.3%
October 2018	3.3%
Indexation factor from March 1982:	
Frozen at December 2017	2.501

Interest on overdue tax

Interest on all unpaid tax is charged at the same rate.

The formula is Bank base rate plus 2.5% which gives a present rate of 3.25% from 21st August 2018

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.75% from 13th August 2018

Repayment supplement

Interest on overpaid tax is payable at the same rate from 21st August 2018

The formula is Bank base rate minus 1% but with an overriding minimum of 0.5% which applies at the present time.

Except IHT where the rate is 0.75%

Official rate of interest

To 6th April 2014: 4%

To 6th April 2015: 3.25%

To 6th April 2017: 3%

From 6th April 2017: 2.5%

IHT: Business Property Relief

It is well known that HMRC are reluctant to allow business property relief for inheritance tax where the business is that of letting property. They have consistently taken the view that the letting of property is a business which consists wholly or mainly in the making or holding of investments, no matter how extensive the services which are provided.

The recent decision in *Marjorie Ross v HMRC TC5959* which I mentioned in the April Tax Bulletin, gives a considerable degree of hope because the services provided in that case were sufficient to allow the relief to be given.

There was also the case of the *Executors of Vignes v HMRC TC6068* which concerned a livery business. Land and buildings are naturally an important part of any livery business and HMRC took the view that, for that reason, business property relief was not available because the business was that of letting or licensing of land; it was therefore a business of making or holding investments.

The Tribunal did not accept this view and rejected all the arguments of HMRC saying that no properly informed observer could have concluded that the business was that of holding investments. They described the view of HMRC as a wholly artificial analysis.

I said before, but it is worth saying again, that it is difficult to resist the observation that HMRC chose to advance a wholly artificial analysis in an attempt to win their case. This is behaviour which they regard as absolutely unacceptable and deserving of serious penal sanctions if it is done by anybody else.

Under the circumstances, it was inevitable that HMRC would appeal. The Upper Tribunal have now heard this case and concluded that the FTT were right in allowing the relief. They said that the FTT applied the correct legal test and their decision should not be disturbed. This is an important decision because although decisions of the First Tier Tribunal have no precedential quality, those of the Upper Tribunal are binding on the lower courts just like decisions of the High Court. Accordingly, the confirmation that the FTT expressed the correct legal test in *Vignes* provides us with the benchmark for this relief for the future.

A crucial point here is that the only other Upper Tribunal case on the subject was that of *Pawson [2013] UK UT 50*. The test laid down in *Pawson* was criticised by the

FTT in *Vignes*. The FTT said that the Upper Tribunal had started from the preconceived idea that the business was the making or holding investments and then asked whether there are factors indicating to the contrary. The FTT said that the proper starting point is to make no assumption one way or the other, but to establish the facts and determine whether the business is wholly or mainly one of making or holding investments.

The judgment reveals that in refusing leave to appeal in *Pawson*, the Court of Appeal had said there is no presumption that business which consists of the exploitation of land for profit is an investment business. It is odd, to say the least, that HMRC chose to continue to argue the point.

Protected Trusts: OIGs

The CIOT / ICAEW have been working hard making representations to HMRC regarding the Trust Protections introduced to relieve some of the worst features of the non dom tax rules which were introduced in 2017.

Where an individual becomes deemed domiciled in the UK under the 15/20 years test, any trust previously established by that individual can benefit from the trust protections. This means that the settlement provisions and the transfer of assets abroad provisions whereby the income of the trust would be treated automatically as that of the settlor, are turned off – providing there are no distributions from the settlement. (You can also lose protection if you monkey around with your trust, but that is another story).

The professional bodies have been explaining to HMRC that the legislation relating to offshore income gains (that is to say gains realised on the disposal of non-reporting funds) do not qualify for the trust protections and are taxable whether they are held by trustees or not.

There seems to be no good reason why offshore income gains should not be protected under the legislation. The whole idea is that they should be protected – but they are not.

Nevertheless, representations to HMRC on this point have not been effective. They say that a decision has been made not to amend the rules to protect offshore income gains. The reason is that "the current demands placed on Parliamentary resources make it difficult for the government to justify returning to the legislation at this time". Funny that. There never seems to be any shortage of Parliamentary time to deal with things of amazing triviality which give rise to additional income.

CGT: Main Residence Exemption

Another case on the subject of the private residence exemption has been heard by the First Tier Tribunal which regrettably adds to the confusion surrounding this exemption: *Yechil v HMRC TC 6829.*

Mr Yechil made a claim for capital gains tax exemption under section 222 TCGA 1992 in respect of a gain made on his private residence. He was no doubt advised, or had regard to, the plethora of previous decisions on this subject.

The key issue is of course whether the property was his only or main residence; it obviously has to be a residence before it can be a main residence. We know from Lord Widgery in *Fox v Stirck* that a residence for this purpose means:

- The place where a man is based or continues to live;
- Where he sleeps, shelters and has his home;
- Something other than temporary accommodation;
- There is some expectation or continuity with a degree of permanence.

Mr Yechil may have had regard to the case of *David Morgan v HMRC*. Mr Morgan was purchasing a property where he intended to live when he and his fiancée were married. He had sold his own flat and moved in with his fiancee's family – but unfortunately two weeks before the purchase of the property the relationship ended, and he went to live with his parents. He carried on with the purchase of the property and moved in for two weeks specifically to repair the house for renting and then moved back to live with his parents. The property was let and eventually sold. The Tribunal decided that Mr Morgan had lived in the property for two weeks and that was enough for it to qualify as a residence.

Mr Yechil may also have had regard to the case of Dutton-Forshaw v HMRC TC 4644. The issue in that case was whether the property in which Mr Dutton-Forshaw had lived for 7 weeks from 5th August to 25th September 2006 was his only or main residence. Having regard to the obvious temporary nature of the accommodation one might have thought HMRC were on strong ground for claiming that this was not a residence at all. However, the Tribunal said that if this was not his residence, he would have had no property which was his residence during the period and they thought this would be a surprising result. Accordingly, they decided that although he only lived in the property for 7 weeks, there was sufficient permanence or continuity for it to have been his main residence.

In the case of Mr Yechil, he bought a property at Beaufort Drive in September 2007 with the intention that it would be the family home for him and his fianceé. The property needed a significant amount of work and while this was going on, they lived in a one bedroom flat elsewhere. They got married, but in January 2011 the marriage came to an end and in April 2011 he moved into the property at Beaufort Drive. In October 2011 the property was advertised for rent and sale; in December he moved back to live with his parents and in August 2012 the property was sold.

There seems to be no dispute that Mr Yechil lived there until he moved back to his parents, although the accommodation was rather unsatisfactory. It had a bedroom and a kitchen and a bathroom. He slept there every night between April 2011 and July 2011 although it is not clear what happened after July 2011. He did not cook there (he did not cook at all it seems) and had meals at his parents' house or had a take away. He did eat at the property, sometimes standing up, sometimes in his car, and sometimes in bed. He received post at the property, but took his clothes to his parents for washing. (I wonder if life like this rings any distant bells with anybody?)

The Tribunal noted that he clearly spent significant periods of time during the day at his parents' house. However, the Tribunal said that as well as occupation, and an intention to occupy for a time with a reasonable degree of permanence, the quality of his occupation must be determined by what he actually did in the house. They considered that to have the quality of residence, the occupation of the house should not only constitute sleeping, but also periods of cooking, eating meals sitting down and generally spending some periods of leisure there. (Mr Yechil might wonder where these new tests come from).

It is clear that Mr Yechil's living arrangements were rather unsatisfactory compared with those of people in rather better circumstances and the fact that he ate his take away meals in bed, or standing up and not sitting down, seems a rather bizarre criterion on which to base whether somebody was living in the property.

It might be said that many people live in difficult circumstances about which Tribunal members might say "you cannot live like that" – but some people have to, because they have no choice. They eat their meals in bed or standing up because they cannot afford a table – or perhaps not one big enough for all the family. It may be questionable that somebody should be denied the main residence relief for this reason.

If we look at the tests set out by Lord Widgery in *Fox v Stirk*, Mr Yechil would seem to satisfy all of them – and he would have the support of previous cases such as those mentioned above. Admittedly, there are other cases where the Tribunal has come to a different view, but that does not mean this case does not have considerable support.

This would seem to be the first case to have been decided on the basis of the unsatisfactory nature of a person's lifestyle rather than the established criteria.

Schedule 36 Notices

A notice under Schedule 36 Finance Act 2008 is a statutory notice to require the taxpayer to provide information and documents which are "reasonably required by the officer for checking the taxpayers tax position". It does of course carry penalties for non compliance.

The power to seek such information is important to HMRC to enable them to obtain the necessary information to ensure that a taxpayer's affairs are correct – particularly in the context of self assessment.

However, as with any statutory power there is the risk of it being used inappropriately.

The taxpayer can appeal against a notice in the normal way if he considers that the requirements for the issue of such a notice are not satisfied – which is often that the information or documents requested are *not* reasonably required for checking the taxpayer's tax position.

Two recent cases throw an interesting light on such notices. In both cases HMRC considered that the taxpayers lifestyle gave them grounds to believe that there had been omission from their tax returns. In one case *Newton v HMRC TC 6682* the Tribunal decided that the request for information was unjustified and it was set aside (with incidental reference being made to the relevant time limits which seemed to preclude a notice anyway). In the other case, *Holmes and Knight v HMRC TC 6824* the Tribunal decided that the statutory notice was justified – although interestingly no reference to the time limit was made in this case.

Although the facts in each case were different (of course) there are sufficient similarities to suggest that the reasoning may be flawed in one of them. The question is which one?

Discovery Assessments

The possibility that a discovery can become stale, causing it to go out of time – even if the statutory time limit has not expired – thereby precluding HMRC from raising a discovery assessment, continues to engage the attention of the courts.

It can now reasonably be concluded that a discovery can become stale and that HMRC cannot just:

> "Sit on it and do nothing for a number of years before making an assessment just before the end of the limitation period".
>
> *Pattullo v HMRC (2016) UKUT 0270.*

This follows the Upper Tribunal decision in *Charlton v HMRC (2013) STC 866* and that the assessment must be issued whilst it retains its essential newness.

In *Gordon v HMRC TC 6537* the tribunal found that the discovery was stale and that a delay of 2 years was too long for the discovery to retain its essential newness. And in *Tooth v HMRC TC 5452* the Upper Tribunal held that HMRC must act expeditiously in issuing an assessment when they have made a discovery.

However, despite all this, HMRC are undeterred. In the case of *Beagles v HMRC (2018) UKUT 0380,* faced with a delay of 2½ years from making the discovery to raising the assessment, HMRC simply argued that all these cases were wrong. They failed.

It would seem that in the absence of a Court of Appeal decision to the contrary, this matter must surely now be settled in principle. It will of course depend upon the facts whether or not an assessment is stale in any particular case.

The case, however, does highlight an unsatisfactory feature. No matter how many cases are stacked up against them, it seems that HMRC will continue to argue on the basis that everybody is out of step except them. They should be careful what they wish for. If HMRC can say that all the cases with which they disagree are all wrong, there is no reason why the taxpayer should not do the same. That will give rise to an explosion of unmeritorious litigation which will be in nobody's interests. A more balanced view, based on established legal principles, must surely be preferred to an intolerance to any view contrary to their own.

For the tax authorities to insist that their view must always be accepted (even if the courts disagree) is as short sighted as it is abhorrent – and hardly likely to engender the respect and the compliance which has been a treasured hallmark of the UK tax system.

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