Non-residents CGT returns

Some clarification would seem to be necessary regarding the obligations for submitting non-residents CGT returns and the penalties for failing to do so.

In the case of *P Saunders v HMRC* [2017] UKFTT 765 (TC) (and in *R McGreevy v HMRC* [2017] UKFTT 690 (TC)), HMRC spectacularly failed to impose penalties for the late submission of non-resident CGT returns.

Miss Saunders sold a UK residential property at a loss. She was not resident in the UK and although she was aware that CGT can now be charged on non-residents who sell UK residential property at a profit, she did not know that it was necessary to submit a CGT return within 30 days of completion of the sale, even if she made a loss – failing which there would be a penalty. Bad luck.

Well, actually not bad luck; she should have known, and there was no excuse for not knowing, and please find enclosed a penalty of £1,300 which you might regard as a sort of aide-mémoire. HMRC is all heart. I think it is called customer service.

However, the tribunal took the view that Miss Saunders had no obligation to submit a non-resident CGT return at all. The reasoning was that you have to make a return if you are the 'taxable person'; that is, the person who would be chargeable to CGT in respect of the gain. In this case, the appellant made a loss and was not therefore a 'taxable person' because there was no gain.

The tribunal went on to consider whether or not Miss Saunders would have had a reasonable excuse to relieve her from the penalty, even if she did have an obligation to file a non-resident CGT return.

HMRC argued that she had no excuse on the following grounds:

- non-resident individuals have an obligation to stay up to date with legislation in the UK;
- ignorance of the law is no excuse and she should have been aware of the changes effected by TMA 1970 s 12ZB; and
- the obligation to file a non-resident CGT return within 30 days of completion of the sale is not obscure or complex law.

Er, no, No and NO. The tribunal rejected all these arguments for reasons similar to those expressed in *R McGreevy* – not least the view of Judge Thomas that HMRC's suggestion was 'claptrap' (a technical term derived from classical texts) and that the idea that the new legislation was not obscure or complex was 'preposterous'.

The tribunal even pointed to the fact that in its published materials on this subject, HMRC explained the requirements incorrectly – which rather supports the proposition that the law must be obscure or complex if HMRC did not get it right itself.

An appeal would seem to be likely but, in the meantime, there has been a further decision from the FTT – *Hesketh v HMRC* [2017] UKFTT 871 (TC) – where the tribunal upheld a penalty for the non-submission of the non-resident CGT return, taking the view that the cases of *R McGreevy* and *P Saunders* were wrongly decided. This might be said to be further evidence that the law is obscure or complex if even tribunal judges get it wrong.

It is difficult to know how the taxpayer (or non-taxpayer) is supposed to fulfil their tax obligations when faced with these conflicting decisions. The imposition of penalties in the light of such uncertainties do nothing to enhance the public perception of the fairness of the tax system or of those who are responsible for its operation. Some clarification or a sensible practice statement would clearly be welcome. ■

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Can the novation of a contract be a supply of land?

***Hanuman Commercial Ltd v HMRC* considered whether novation of a contract for the sale of land was an exempt supply of land or a separate supply of services for VAT purposes.**

What is novation? In essence, a novation has the effect of replacing one party to a contract with a new party. Novation takes place when one party to a contract releases the other contracting party from its contractual obligations in consideration for a third party assuming those obligations.

The facts in this case: In *Hanuman Commercial Ltd v HMRC* [2017] UKFTT 854 (TC), Sabre Insurance Company Limited (Sabre) entered into the original contract for the sale of a property (the 'Sabre contract') for £2.8m with Hanuman Commercial Limited (HCL). Before completion, HCL entered into a contract with Connect Centre Limited (CCL) for the onward sale of the property for £5.5m (the 'CCL contract'). A number of subsequent agreements varied these two contracts.

Essentially, the result was that by a deed of novation between the three parties, HCL's rights and obligations under the Sabre contract were novated to CCL so that CCL would acquire the property from Sabre. On completion, CCL paid £2.8m to Sabre and £2.7m to HCL (to make up the total consideration of £5.5m).

HCL had initially purported to charge VAT on invoices it issued to CCL but subsequently decided that VAT was not properly chargeable. HMRC disagreed and issued an assessment for this VAT. HCL then appealed against the assessment.

The judgment: HCL argued that it had made an exempt supply of an equitable interest in the property to CCL, as it was obliged to do under the CCL contract. The VAT treatment should follow the economic reality of the transaction, which was that there was a transfer of an interest in the property from HCL to CCL.

HMRC's position was that the exemption did not apply because HCL did not supply a freehold interest in the property to CCL. The original contract between Sabre and HCL was novated and thus, the property went directly from Sabre to CCL. CCL was paying HCL to step away from its contract with Sabre rather than to transfer the property to it.

Judge Robin Vos found that, prior to the novation, HCL did have an equitable interest in the property and an obligation to transfer this interest to CCL under the CCL contract. However, the effect of the novation was to 'rip up' the original contract with the result that it was as if it had never existed and HCL's obligations under it fell away.

Instead, under the novation agreement, HCL granted CCL the right to enter into an agreement with Sabre to purchase the property. The grant of this right was not an exempt supply of land but a supply of services. VAT was due on the supply of services, which was standard rated in this case.

Conclusion: Novations are often a problematic area of law. As it stands, in the case of a contract for the sale of land, a novation is to be treated as a separate supply from the underlying supply of the land and may therefore be subject to different VAT treatment.

In this case, part of the rationale for novating the contract, rather than the land being transferred from Sabre to HCL and then on to CCL, was to ensure that the transaction would be treated as a transfer as a going concern for VAT purposes (and therefore outside the scope of VAT).

The judge remarked that, since it was intended that the novation should alter the VAT treatment of the transaction in general, it was not surprising that it also altered the VAT treatment of the supply by HCL. ■

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