UK Tax Bulletin

June 2020

FIELD COURT TAX CHAMBERS

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Latest Rates of Inflation and Interest

The following are the latest rates: June 2020

Current Rates	
Retail Price Index: April 2020	292.6
May 2020	292.2
Inflation Rate: April 2020	1.5%
May 2020	1.0%
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 rate of 2.6% from 9th April 2020.

There is one exception: Quarterly instalments of corporation tax bear interest at only 1.25% from 23rd March 2020

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.

Official rate of interest

To 6th April 2015: 3.25%

To 6th April 2017: 3%

To 6th April 2017: 2.5%

From 6th April 2020 2.25%

IHT: Excluded Property Trusts

Apart from the provisions setting out how the grants to support business during the crisis are going to be subject to tax, and all the stuff about exceptional circumstances, the Finance Bill has some really troublesome changes to inheritance tax and excluded property trusts.

Although they have insisted that the changes are not retrospective, they quite clearly are – and they are going to catch lots of people unawares. This is deeply unfair and we can only hope that the sterling efforts of the professional bodies in highlighting the position will bear fruit.

The first proposal is that where a settlor who had created a settlement when he was not domiciled, later becomes domiciled or deemed domiciled, any subsequent additions to the trust will not be excluded property in the hands of the trustees.

HMRC have long taken the view that this was the case anyway. It wasn't – but it is now.

The problem arises with the second proposal which relates to transfers from one excluded property trust to another at a time when the settlor has become domiciled or deemed domiciled. Why should this be an issue? I don't know but the property transferred will be denied excluded property status.

However, although it does not make much sense, the settlor can at least avoid the difficulty providing he appreciates that this would be the effect of the transfer. But what if the transfer took place years ago. The property is now retrospectively treated as non- excluded property and there is nothing he can do about it. It is now subject to the 10 year charge and exit charges and moreover will form part of the settlor's estate if he is a beneficiary – which in many cases he would be. The settlor could exclude himself from benefit to avoid the death charge from the reservation of benefit – but that will simply give rise to a PET which will be chargeable if he dies within 7 years.

Goodness me that is unfair.

As I mentioned last month in my comments on a new book charting the history of tax over the centuries (and indeed millennia), taxes which are perceived to be seriously unfair sow the seeds of discontent and have ended up with disastrous consequences – how about the Poll Tax or the American Civil War, the Boston Tea

Party …. the list is rather long.

However it is perhaps unlikely that the proposed changes to the IHT treatment of excluded property trusts will cause the population to rise up and storm Parliament – but it is still not right.

Exceptional Circumstances: Residence

The Finance Bill also includes the detailed legislative changes regarding the days in the UK which can be disregarded on the grounds of exceptional circumstances because of the coronavirus. They are accompanied by a Technical Note.

These provisions are a bit disappointing because the relaxations are extremely narrow – although to be fair, they are no narrower than were suggested in the letter from the Treasury of 9th April. In that letter the Chancellor explained that the Statutory Residence Test would amended to ensure that any days spent in the UK during the relevant period by individuals who are "working on COVID-19 related activities" will not count towards the residence tests.

The Finance Bill provides that the relaxations apply to individuals who are:

a) Not UK resident for 2019/20

b) Tax resident in another jurisdiction

c) Medical or healthcare professionals who are in the UK for purposes connected with, (or the development of products such as vaccines for) the detection, treatment or prevention of the virus.

These rules only apply to disregard days during the period from 1st March to 1st June 2020 and there is no increase in the absolute 60 day limit on exceptional days.

Anybody able to claim this relief will clearly deserve it – but I doubt whether it will apply to many people.

The other relaxations announced by HMRC on 9th March on their interpretation of "exceptional circumstances" are not affected - but they were merely interpretations by HMRC and did not need any amendments to the legislation.

At a recent Zoom seminar it was emphasized that arguments regarding exceptional circumstances resulting from the lockdown and all the associated restrictions connected with the virus, may have been long forgotten when the matter comes to be argued in two or three years' time. Accordingly, it would be a wise move to ensure that all available evidence is collected now, whilst it is available, to demonstrate that exceptional circumstances existed – and were within the HMRC relaxed guidelines. Good advice, I think.

Exceptional Circumstances: SDLT

The Finance Bill also includes a relaxation to the 3% SDLT surcharge and the possible application of exceptional circumstances to the time limits.

Where a person buys a new main residence before they have sold their old main residence they are obliged to pay the 3% surcharge. However, they are entitled to a refund if they sell their existing main residence within three years: schedule 4ZA(3)(7)(b) FA 2003.

The Government acknowledge that there have been difficulties in attempting to sell properties during the restrictions caused by the virus. Accordingly, where the new residence was purchased on or after 1st January 2017 the purchaser will still be entitled to a refund if they sell the previous main residence within the permitted period, which is:

> "such longer period as HMRC may allow is satisfied in response to an application that the sold property would have been disposed of in the 3-year period if the disposal had not been prevented by exceptional circumstances that could not reasonably have been foreseen"

HMRC say that exceptional circumstances would include being prevented from selling the property owing to Government guidance during the Covid-19 pandemic or other action taken by a public authority preventing the sale of the property.

I was not aware that there was any specific Government guidance preventing the sale of properties. The circumstances behind this relaxation will almost always involve somebody who has sold their main residence and moved into their new one but were unable to sell their previous residence which presumably would not then be occupied.

One can understand that it may be difficult to view a house if a person is living there under lockdown circumstances – or is perhaps shielded – but this would have no application if the property is vacant. It may be a bit more administratively difficult but there seems nothing to prevent such a house being sold. "Prevent" would not seem to encompass "less convenient".

Nor am I aware of any action which is being taken by public authority to prevent sales of properties – but I suppose there must be some such circumstances.

HMRC specifically say that a mere change of intention of the parties, possibly as a result of the virus giving rise to a downturn in the market, would not be regarded as an exceptional circumstance.

I would not want to be sniffy about HMRC's wish to assist people in difficult circumstances, but I would be surprised if anybody was actually able to benefit from this relaxation. Perhaps they will adopt their famous "light touch" when it comes to considering such claims.

Sale of Goodwill

The recent case of *Mr and Mrs Pickles v HMRC TC 7681* contains some interesting features.

Mr and Mrs Pickles carried on a business in partnership and for good commercial reasons, decided to incorporate the business. The goodwill of the business was sold to the company for £1.2 million in accordance with a Sale Agreement and a professional valuation. The consideration could not be paid immediately and accordingly, the £1.2 million was credited to their loan account from which some withdrawals were made in due course.

Nothing particular unusual here. I expect that this would have been highly advantageous because the capital gain on the goodwill would have attracted capital gains tax at 10% because of Entrepreneurs Relief – which is no longer available for such transfers after 3rd December 2014.

However, HMRC said the value placed on the goodwill was too high and sought to charge Mr and Mrs Pickles to income tax on the excess consideration on the grounds that it was a distribution.

The Tribunal confirmed the market value of the goodwill at £270,000 – so effectively Mr and Mrs Pickles had sold an asset worth £270,000 to the company for £1.2m.

HMRC said that this excess £930,000 represented a distribution under section 1020 CTA 2010. Section 1020 CTA 2010 provides that where there is a transfer of assets to a company by its members, and the amount or value of the benefit received by the members exceeds the amount or value of any new consideration given by the member, is a distribution.

This looks like a compelling argument. A sale of an asset for more than it is worth is still a sale and immediately chargeable to capital gains tax even though some or all of the consideration remains outstanding. Indeed, that is exactly what section 48 TCGA 1992 is designed for.

However, the Tribunal saw the matter differently. The Tribunal decided that the consideration was the creation of a liability in the form of a debt owed by the company to its members but as Mr and Mrs Pickles received only part of that sum, only the amount received could be treated as a benefit received by the member. Specifically, the Tribunal said:

> "In summary, the argument that by crediting a director's loan account the company made a distribution for the purposes of Section 1020 is misconceived. The transaction creates a liability on the part of the company and therefore there can be no transfer of assets. Alternatively there can be benefit or value to any benefit accruing to the members from such a transaction for the reasons given above.
>
> To the extent that the debt was paid by [the company] and this sum exceeds the value of the goodwill then that [excess] was a benefit received by Mr and Mrs Pickles and was accordingly a distribution under Section 1020. However, the remainder of the debt which remains outstanding cannot be so regarded. There is no basis for arguing otherwise".

I would respectfully suggest that many people will find there is considerable basis for arguing otherwise.

Quite apart from the general legal analysis, the question can be distilled into whether the crediting of an amount unreservedly to the director's loan account represents payment for relevant purposes. The Tribunal said it did not – they said the very idea was misconceived - but this rather conflicts with the decision in *Garforth v Newsmith Stainless Ltd (1979) STC 129* which held precisely that the placing of sums unreservedly at the disposal of a director by credit to his loan account was payment for tax purposes.

It is a very attractive idea that the consideration for a sale is not taxable until the money is actually received and it will be interesting to see what the Upper Tribunal says about it.

Bare Trusts

The recent case of *Bhikhi v HMRC TC 7728* contained a detailed analysis of whether an asset is held on a bare trust.

What happened in this case is that the taxpayer transferred a property to a company for the price of £499,000. The company obtained a mortgage for approximately half the consideration and the balance was left outstanding. This gave rise to a claim by HMRC for capital gains tax on this disposal. Well, yes. This has a strangely coincidental resonance with Mr and Mrs Pickles referred to above.

The taxpayer (who clearly had not thought of the *Pickles* defence) disputed the charge to capital gains tax on the grounds that the company was holding the property as bare trustee for him and he retained the beneficial ownership.

There were plainly a number of difficulties with this argument and it did not find favour with the Tribunal. The judgment contains an extensive explanation regarding the requirements for a disposition of land, the circumstances when property is held as nominee or on bare trusts under section 60 TCGA 1992 and whether there was any implied or constructive trust.

This is all very interesting (if you are interested in that sort of thing) and well worth a read. None of it helped Mr Bhikhi who failed to show that any of the relevant conditions for the existence of a bare trust were satisfied.

Actual or Notional Transactions

In the recent case of *Boston Khan v HMRC 2020 UK UT 0168* the taxpayer received a payment from a company following a repurchase by the company of its own shares.

HMRC argued that the buy-back of shares was a distribution taxable under section 383 ITTOIA 2005. Mr Khan claimed that the purchase and sale of shares in the company was a trading transaction and that the disposal of shares amounted to a disposal of trading stock. He lost.

The reason I mention this case is because of the interesting paragraph 99 in which the Tribunal say as follows:

> "In our view, it is plain that Mr Khan received the distribution and was entitled to receive it. ….. He is to be taxed in accordance with the transaction that he did enter into and not by reference to the transactions that he was about to enter into (but did not) even if they might have left him in the same economic position".

I would respectfully say that this statements seems wholly right – or at least it ought to be. Unfortunately, exactly the opposite applies for Stamp Duty Land Tax purposes where the taxpayer is able to be taxed, not in accordance with transactions that he entered into, but by reference to transactions that he did not enter into, (and had no intention of entering into) even though they left him in the same economic position.

I do not suggest that the SDLT position is incorrect – the Supreme Court tells us that this is exactly in accordance with the law as expressed in section 75A FA 2003. Nor do I suggest that the decision in Boston Khan is incorrect – but the general proposition articulated by the Upper Tribunal that a taxpayer is not to be taxed on the basis of a transaction which he did not enter into, perhaps goes a bit too far.

Or maybe it doesn't. Maybe it is right, and it is a principle which we can embrace.

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30th June 2020

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