FIELD COURT TAX CHAMBERS

Actual or notional transactions[1]

We should be taxed on the transactions we undertake, not on notional ones that we do not.

In the recent case of *B Khan v HMRC* [2020] UKUT 168 (TC), the taxpayer received a payment from a company pursuant to a repurchase by the company of its own shares.

Mr Khan had bought all 99 of the issued shares of a company from the other shareholders for £1.95m plus the net asset value. On the same day the company immediately bought back 98 of the 99 shares for £1.95m leaving Mr Khan with one share in the company.

HMRC argued that the buy-back of shares was a distribution taxable under ITTOIA 2005 s 383. Mr Khan argued in vain that his purchase of shares in the company and the subsequent purchase by the company of their own shares was a trading transaction, and that his disposal of shares amounted to a disposal of trading stock. The tribunal did not think so.

The question then arose as to whether the transactions should be treated as a single composite transition, so that Mr Khan should simply be treated as acquiring the one share he ended up with. The tribunal acknowledged that the transaction could have been structured in a different way – but it wasn't.

I mention this case because of the interesting paragraph in the decision (para 99) where the Upper Tribunal says that:

> "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 transactions 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 suggest that this statement must be right – or at least it ought to be. We should to be taxed on the transactions we actually undertake, not on some other transaction that we did not.

Unfortunately, exactly the opposite applies in the real world of taxation.

One example would be SDLT where the taxpayer is able to be taxed, not in accordance with transactions that he entered into, but by reference to notional transactions that he did not enter into (and had no intention of entering into) but which 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 FA 2003 s 75A, irrespective of whether there was any tax avoidance motive.

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Another example would be the intermediaries legislation where the taxpayer can be charged to tax on the basis of a notional contract, which he did not enter into, and with a different person.

There are also numerous cases of purposive interpretations that look at the beginning and then at the end and disregard (or recategorise) everything in between. In other areas of law this would be utterly condemned. A father gives £1,000 to his son. On this reasoning, the state could disregard the gift and charge the son with theft on the basis of a notional transaction that he stole the money – or if it prefers, it could treat the son's receipt as taxable income, or as anything really.

Regrettably, it would seem that the general proposition articulated by the Upper Tribunal – that a taxpayer is not to be taxed on the basis of a transaction that he did not enter into – goes a bit too far. Or maybe it doesn't. Maybe it is exactly right, and it is a principle which we are entitled now to embrace.

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