UK Tax Bulletin

November 2020

FIELD COURT TAX CHAMBERS

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Latest Rates of Inflation and Interest

The following are the latest rates:

Current Rates	
Retail Price Index: October 2020	294.3
September 2020	294.3
Inflation Rate: October 2020	1.3%
September 2020	1.1%
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%

Nudge Letters

It may be remembered that a while ago, HMRC came in for some criticism for sending letters to people asking them to fill in a certificate confirming that their tax returns were right and making aggressive sounding noises about penalties. The certificate was completely unlimited and therefore covered all years.

The professional bodies made a lot of fuss about this and pretty much advised people not to sign the certificate as there was no legal obligation on them to do so. Nevertheless it was generally considered wise to write and explain - if anything needed explaining – to forestall an unnecessary and time consuming section 9A enquiry.

HMRC have recently published details of a new approach which they are about to adopt – the sending of (very gentle) nudge letters. I think they are rather good.

The letters cover a number of subjects:

ATED – the need to file a return to claim relief for a let property

CGT – where a disposal of residential property may have been overlooked

Benefits in Kind – where the company and personal details do not tally

Investment income – where some income may have been overlooked

Possible earnings - for Persons of Significant Control

Essentially the letters say:

- We get lots of information which we try to marry up with the tax returns.
- Can you just check that you have not forgotten anything on your last tax return – for example ….
- If you believe that everything is right then you do not have to do anything.
- You might like to amend your return if there is something wrong.
- This is not a compliance check or enquiry – it is just us trying to be helpful.

All credit to HMRC. Nobody can take exception to these letters or feel intimidated by them. They are genuinely helpful and I am sure HMRC will receive a good (and rewarding) response.

Principal Private Residence

Everybody is familiar with the capital gains tax exemption for the only or main residence in section 222 TCGA 1992. There are lots of technical issues which arise with the exemption but I am concerned here with the basic building block for the exemption: that the property must be a *residence.*

Although that sounds straightforward, all sorts of difficulties seem to arise.

The starting point in all the authorities on this matter is always the judgment of Lord Widgery in *Fox v Stirk [1970] 3 All ER 7* who said that "a residence" 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 of continuity with a degree of permanence.

This has been considered by the Courts many times.

Decisions of the Courts and Tribunals are published so as to assist the citizen in understanding the law on a particular subject. Decisions may differ having regard to the particular facts of the case – but the legal principles ought to be clear.

When it comes to the decisions on the exemption for the main residence, clarity seems to be in short supply.

Let us start with the case of *Susan Bradley v HMRC TC2560*. Mrs Bradley lived in a house which she owned jointly with her husband. She also owned another small house which was normally let. She decided to leave the matrimonial home and moved into the small house when it became vacant in April 2008, making various improvements and generally making it her home. Although the property was on the market, the market was very poor and she expected to live permanently in the property. However, Mr and Mrs Bradley later became reconciled and she moved back to the matrimonial home in November 2008. She sold the small house in January 2009.

During the period April 2008 to November 2008 she lived in the small house and probably felt confident that the property would qualify, not only as her residence, but as her main residence.

The Tribunal decided that the property was not Susan Bradley's residence at all. They said that she never intended to live permanently in the property; it was only ever going to be a temporary home and it was therefore never her residence.

The Tribunal was heavily influenced by the Court of Appeal judgment in *Goodwin v Curtis [1998] STC 475* where it was held that the occupation of the property must show some degree of permanence and some expectation of continuity– which were two of Lord Widgery's tests in *Fox v Stirk*. However, in *Goodwin v Curtis* the taxpayer had separated from his wife and family, stayed in the property as temporary accommodation – and after only two days he completed the purchase of another property which was intended to be his private residence.

It was a bit of a stretch to suggest that Mr Goodwin occupied the property as his residence; it was obviously the most temporary of accommodation. This is a long way from the situation of Mrs Bradley who moved into a perfectly suitable home, took steps to make it more of a home and lived there from April to November without any intention of moving out unless the house were to be sold which was unexpected.

Mrs Bradley may have thought herself a bit unlucky with the outcome of her case – but maybe she accepted that she was not really there long enough for it to be her residence. However she would have been seriously enraged by reading the case of *David Morgan v HMRC TC 2596* which was published only three weeks later.

Mr Morgan was getting married. He was in the process of purchasing a property which would be the matrimonial home. He was living with his fiancée's family but unfortunately two weeks before the purchase of the intended matrimonial home, the relationship ended. So he went to live with his parents. Nevertheless he carried on with the purchase of the property and moved in for two weeks specifically to prepare the house for renting and then moved back to live with his parents. The property was let and then sold. He claimed the exemption – to which many might have thought: You Cannot be Serious! However, the Tribunal decided that Mr Morgan had lived in the property for two weeks and this was enough to qualify it as a residence.

Then we have the case of *Piers Moore v HMRC TC 2827*. Mr Moore also had matrimonial difficulties and moved into another property taking furniture with

him from the matrimonial home. He took all his clothes knowing that he would never return. He lived there from November 2006 to July 2007 spending pretty much every night there except when he was away on business. The Tribunal found that he did not occupy the property with a sufficient degree of permanence for it to be a residence. It was only temporary accommodation.

Then we have the case of *Dutton Forshaw v HMRC TC 4644*. Mr Dutton Forshaw had owned and lived in loads of properties. In the end the issue was whether the property in which he had lived for seven weeks was a residence. In these circumstances, one might have thought that HMRC were on strong ground in claiming that this was not a residence at all but merely temporary accommodation. However, the Tribunal took the view that if this was not the taxpayer's residence for that period he would have had no property which was his residence and they thought that would be surprising. Accordingly they decided that there was sufficient permanence or continuity for his seven week period of occupation for it to be his residence and his main residence.

Susan Bradley would by now have disappeared into a slough of despond. There she would probably have found Piers Moore – and also Mr Yechil.

Mr Yechil had claimed the exemption too: *Yechil v HMRC TC 6829*. He bought a property in September 2007 with the intention it would be the family home for him and his fiancée. It needed significant 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 intended property. In October 2011 the property was advertised for rent and sale; in December he moved back to live with his parents and sold the property in August 2012.

There was no dispute that Mr Yechil lived there although the accommodation was rather unsatisfactory. It had a bedroom, a kitchen and a bathroom and he slept there every night between April 2011 and July 2011 although it is not clear what happened after July. He did not cook there (he did not cook at all it seems) and had meals at his parents' house or had a takeaway. He had meals at his 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; (this rings a distant bell).

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 involve sleeping,

but also periods of cooking, eating meals sitting down and generally spending some periods of leisure there. It is not clear where the authority for these additional conditions comes from.

Clearly Mr Yechil's living arrangements were unsatisfactory compared with people in rather better circumstances, but the fact that he ate his takeaway meals in bed or standing up seems a rather bizarre criterion on which to base whether he was living in the property. The Tribunal members might have thought "you cannot live like that" but some people have to. They eat their meals in bed or standing up because they cannot afford a table – or perhaps not one which is big enough for all the family.

With all the above in mind, I turn to the case in October of *Core v HMRC TC 7917*.

Mr and Mrs Core bought a property in Green Lane. They did not move into Green Lane immediately because they were doing building work. They moved into the property in March or April 2014 and they were soon approached by somebody who made an offer for the property. They rejected the offer– and did so again when the offer was repeated. However, about a month later, the purchaser made a higher offer which Mr and Mrs Core decided to accept. They had occupied the property for 6 weeks and the Tribunal found that this was enough to represent a residence, as they had moved into the property expecting to live there for an indefinite period.

I could go on. There are many other cases on this subject.

In any kind of litigation, there always opposing views, but the idea is that a coherent body of authority is built up to assist our understanding of the meaning of complex legislation. Nowhere is this more important than in taxation where the State has a legislative right to deprive citizens of their money.

It is really unhelpful (and wasteful) for confusion to exist. If HMRC and the taxpayer both have a long list of authorities on their side because of the contradictory nature of Tribunal decisions, this merely promotes litigation. The taxpayer will clearly be encouraged to fight his case when he has loads of similar cases which directly support his claim – and you cannot blame HMRC for opposing him if they have loads of cases which directly support their position. And, as can be seen, the outcome is utterly unpredictable – and sometimes inexplicable.

We urgently need some definitive guidance from the superior courts here. As things stand one might question the value of publishing First Tier Tribunal cases – particularly as they do not have any precedential authority anyway.

EMI Approval

This saga has at last come to an end.

In 2018 HMRC published a worrying statement explaining that State Aid approval for EMI schemes by the European Commission was set to expire on 6th April 2018 and that EMI options granted after that date may not qualify for the normal tax benefits.

Fortunately the EC subsequently confirmed that their approval continued while we remained a member of the EU.

This was followed in February 2020 by a statement from HMRC that EMI schemes would continue to be effective until the end of the transition period on 31st December. There seems to be a certain logic to all this – whether we like it or not.

In their Employment Related Securities Bulletin 37 (October 2020) HMRC now confirm that EMI schemes will continue to be effective after 31st December 2020.

This is a relief because EMI schemes are a very valuable opportunity for rewarding employees. No income tax charge on the grant of the option, nor on exercise, nor on sale of the shares. Furthermore capital gains tax will usually apply at only 10% as Entrepreneurs Relief (Business Asset Disposal Relief) is likely to apply.

Carrying on a Trade

It is a well-known anomaly that the meaning of *trade*, which is important to so many aspects of income tax (and numerous other taxes), is not defined in the legislation. The best we have is section 989 Income Tax Act 2007 and section 1119(1) CTA 2010 which both say that: "trade includes any adventure in the nature of trade"

It is therefore no surprise that there have been an enormous number of cases on the subject of whether somebody is carrying on a trade and although they all turn on their individual facts, some important principles have emerged.

In *Ransom v Higgs (1974) STC 539* Lord Wilberforce said that when Parliament introduced the reference to trade in 1799, they wisely abstained from defining it

and left it to the Courts to say what it means. Well, they certainly did that.

There are, of course, the famous badges of trade set out in the 1955 Royal Commission (examined in detail in *Marson v Morton 59 TC 381*), and each one of them has had its own gloss placed upon it by the Courts.

One of the current issues relevant to this subject arises from the Annual Tax on Enveloped Dwellings. This is because ATED is not chargeable where the person entitled to the interest in land is carrying on a property development trade and the land is held exclusively for the purposes of developing and reselling the land in the course of the trade: Section 138(1) FA 2013.

The reason for my sudden interest in this subject is the recent case of *Hopscotch Limited v HMRC [2020] UKUT 0294 (TCC)* in which the taxpayer claimed relief from ATED on the basis that he was carrying on a trade. The FTT decided that he was not, and the matter fell to be considered by the Upper Tribunal.

The case is interesting because of its novelty. The arguments are nearly always the other way round - with HMRC arguing that the taxpayer is carrying on a trade so that the profit is chargeable to tax as income. In this case, HMRC were arguing that they were not – because carrying on a trade would entitle the company to relief from the ATED charge.

One of the areas of occasional difficulty is where an intention to trade is formed after the purchase of the relevant asset. It will sometimes be the case that an asset is acquired for the purposes of investment (or in the case of a property, perhaps for private use) but later an intention to sell is formed. The question arises whether a trade has been commenced so that there would be an appropriation to trading stock (with CGT consequences under section 161 TCGA 1992). There is no doubt that this can occur (see *Taylor v Good 1974 STC 148*) – but if there is no pre-existing trade, there needs to be evidence that a trade has been newly set up; this has to be more than merely taking steps simply to enhance the value of the asset: see *Simmons v IRC 1980 STC 350*

This was exactly the issue in Hopscotch Ltd.

The company had a property (not held as a trading stock) which they decided to sell. It would not sell, so after consulting with advisers they decided it should be totally redeveloped because the redevelopment opportunity would result not only

in a sale but in additional profits from the development.

Accordingly they took detailed advice from numerous advisers relating to the development, sought planning permission and borrowed the money to finance the cost of the work.

These are just the sort of facts which HMRC would normally argue vigorously that a trade had been commenced. However, in *Hopscotch*, they said that this was nothing more than the company taking steps to enhance the value of the property prior to sale. HMRC argued that the work involved in redeveloping the property was not enough to represent a trade; the work was similar to that routinely undertaken by owners of land not carrying on a trade.

The FTT held that the facts did not support the conclusion that a trade had commenced. The Upper Tribunal upheld their decision.

It will be interesting to see what happened when these arguments are deployed by the taxpayer in the future. There is of course no assurance that HMRC will accept this reasoning when used against them in another case, but this looks like a decision with seriously helpful possibilities.

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Important Note