Taxing matters

Peter Vaines explores the ins and outs of non-residents capital gains tax

IN BRIEF

- The rules for the non-residents capital gains tax are clarified.
- The Upper Tribunal comes to the rescue on partial surrenders.
- The High Court allows rectification on grounds of equitable mistake.

We now have the non-residents capital gains tax in place and I think we can be sure it will never go away. Taxes rarely do (although I do remember development land tax being abolished in 1985).

Most non-residents who have an interest in a UK residential property will now be liable to capital gains tax on its disposal. This might catch out a few non-residents because it will also apply to disposals by way of gift and to deemed disposals. We know all about those concepts here, but they might come as a shock to some foreign owners who are unfamiliar with the principles of UK tax.

However, the tax will only be chargeable on the increase in value from 6 April 2015. This will be done either by rebasing or by an election for time apportionment. A frequent question is whether the client should obtain a professional valuation on 6 April 2015 for the purposes of the new charge.

HMRC recommend a professional valuation at 6 April 2015 but there are serious doubts whether this is worthwhile. HMRC will do their own valuation anyway and if you have a contemporaneous professional valuation that does not in my experience cut much ice with them at all (although it may help you avoid a penalty if there is a serious dispute later on).

These days, all property transactions are able to be found on the internet so it should not be a problem because the value can be identified a long time after the event by reference to similar transactions in the same vicinity at the same time. After all, that would be the basis for a professional valuation too (I am not quite sure about the extent of judicial notice here: "it's Zoopla my Lord, innit").

If there is some reason why the property is worth more than normal, perhaps because of some special feature which might be lost in the mists of time, clearly some contemporaneous evidence of these factors would be sensible.

We are still no clearer about how this tax is going to be collected. HMRC explains that the foreign resident, having sold the property will subsequently submit a self-assessment tax return and pay the tax. This looks a bit optimistic—although the increased international cooperation over tax matters now means that recovery action might not be too difficult for HMRC in many cases. We have come a long way since the *Government of India v Taylor* (1955) and the principle that the courts of one country will not enforce the tax debts of another. Double tax treaties, the OECD Convention on Mutual Administrative Assistance and the EU Directive 2010/24/EU in 2010 may give HMRC all they need to collect the tax if somebody is a bit slow in getting round to it.

Tax on partial surrenders

A little while ago, Mr Lobler had a bit of a problem on the partial surrender of a number of life policies. The tax rules worked in such a capricious way that although he made no profit on these policies, an enormous tax liability arose which exhausted his life savings and was going to bankrupt him. The tribunal said this was an outrageously unfair result and it was repugnant to common fairness for HMRC to seek to extract tax in Lobler's circumstances—but there was nothing they could do about it.

Lobler appealed to the Upper Tribunal where HMRC continued to press the argument (*Lobler v Revenue and Customs Commissioners* [2015] UKUT 0152 (TCC), [2015] All ER (D) 14 (Apr)).

Fortunately, Mrs Justice Proudman took a more sympathetic view. She said that when Lobler asked to withdraw some of his funds, the way it was done gave rise to devastating tax consequences, whereas he could have chosen an alternative option which would not have had this effect. Her ladyship said that it is only common sense that nobody would willingly chose the option giving rise to an amount of tax which would bankrupt him (particularly when he had made no profit) if there was a clear choice not to do so.

Lobler sought an order for rectification so that the withdrawal could be regarded as having been undertaken in an alternative manner. The Supreme Court decision in *Pitt v Revenue and Customs Comrs* [2013] UKSC 26, [2013] 3 All ER 429 (recently followed in the case of *Freedman v Freedman & Others* [2015] EWHC 1457 (Ch), [2015] All ER (D) 197 (May)—see below) now makes it clear that rectification is an equitable remedy which can only be granted where the mistake is so grave that it would be unconscionable for the court to refuse relief. Her ladyship considered that the error by Lobler in choosing the partial surrender option was indeed so grave that it would be unconscionable for the court to leave the mistake uncorrected.

The First-tier Tribunal did not have power to order rectification, but the Upper Tribunal did—and did so.

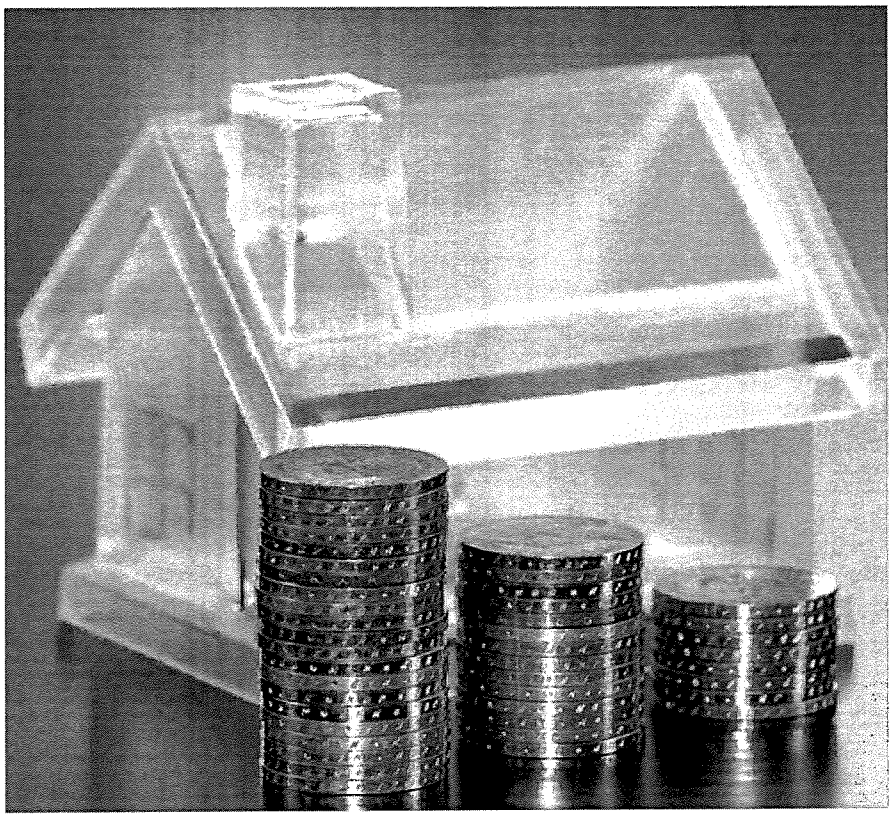
Lobler was just an ordinary taxpayer who invested some money and later withdrew some of it. He was not some arch tax avoider and did not deserve to lose his life savings and be made bankrupt. HMRC are very keen on explaining their duties of care and management of the tax system. I would suggest that not conducting themselves in a manner which the courts describe as "repugnant", ought to be high on their list of priorities when they are exercising their duty.

Group relief

The recent case of *Gemsupa v HMRC* [2015] UKFTT 97 involved a disposal of assets to a third party in such a way as to avoid triggering tax on the capital gain. In essence, the idea was that a transfer of the asset was made to another group company so that the transfer was treated as having taken place at no gain no loss under s 171 of the Taxation of Chargeable Gains Act 1992 (TCGA 1992).

The crucial part of the arrangements required the vendor and the purchaser to be regarded as part of the same group within the complex definitions but without there being any real economic unity. There seemed to be no doubt that the terms of the legislation were satisfied so HMRC argued that the purchaser should not be regarded as part of the group either by applying the *Ramsay* doctrine or by a purposive interpretation of the legislation.

This is not everyday stuff and I mention it only because an important principle



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arose. Where the legislation is precise and prescriptive, the scope for a purposive interpretation is severely limited (this is perhaps confirmed by the case of *Lobler* because he did not succeed on the basis of an alternative interpretation of the offensive provisions, but on the basis of rectification).

In *Gemsupa*, HMRC argued that the satisfaction of the statutory tests by the company should be ignored because the motive was tax avoidance and there was no commercial or economic unity in the structure. In other words, there was a further condition to be satisfied for group relief beyond those set out in the statute. There had to be some form of commercial or economic unity before the group can exist. The tribunal was not prepared to go that far. Nor was it prepared to accept that one of the specific conditions required by the statute (and satisfied by the company) should be disregarded to achieve the result preferred by HMRC.

We might expect this to be exactly the type of arrangement which would engage the attention of the GAAR Advisory Panel. However, that may not prevent HMRC seeking to appeal - or indeed seeking an amendment to the legislation to make it still more prescriptive (and paradoxically making their approach even more difficult).

Entrepreneur's relief

The recent case of *Carver v HMRC* [2015] UKFTT 168 contains an interesting discussion on the concept of an underwriting trade and the nature of "syndicate capacity". Syndicate capacity is the extent to which a syndicate may underwrite insurance business, ie the maximum amount of premium income that it may accept.

Mr Carver was carrying on a trade as a name at Lloyds. He participated in 18 syndicates and sold some syndicate capacity in one syndicate giving rise to a capital gain. Carver claimed that he was entitled to entrepreneurs relief in respect of this capital gain because it was a separate and identifiable part of the business and represented the disposal of part of his business under s 169I(2) of TCGA 1992.

Alternatively, Carver argued that each syndicate represented a separate business so that the sale of his capacity in one syndicate was the sale of that business.

HMRC said that the part of the business disposed of must be a viable part of the composite trade that would still be recognised if it were separated from the whole.

The tribunal decided that the economic activity was the underwriting business, not the holding of syndicate capacity. A name at Lloyds carries on a single trade however many syndicates are involved. The syndicate capacity was the means by which his trade was carried on and although it was an asset of the trade (similar perhaps to goodwill) it was not a trade itself. Accordingly, the gain could not qualify for entrepreneur's relief.

Such a disposal might be thought to represent an associated disposal being a disposal associated with his withdrawal from the business but clearly that did not occur in this case. More importantly, for the relief to apply to an associated disposal under s 169K of TCGA 1992 the business has to be carried on by a company or a partnership. It does not apply to a sole trader.

Equitable mistake

The decision of the Supreme Court in *Pitt v Revenue and Customs Comrs* was pretty much the last word on mistake and on the limits of the *Hastings Bass* principle.

Last year, the case of *Wright v NatWest Bank Plc* [2014] EWHC 3158 (Ch), [2015] WTLR 547 reviewed the guidance from the Supreme Court in deciding whether they were able to exercise their discretion to rescind a disposition on the basis of a unilateral mistake. The High Court said that such a mistake cannot be a pure question of fact nor can it have arisen out of inadvertence or ignorance. The causative mistake must be so grave that it would be unconscionable for the court to refuse relief.

The High Court has again considered this principle (and in particular the observation of Lord Walker who wondered why the courts, rather than the parties' professional indemnity insurers, should have to pick up the pieces when a mistake had been made).

In the case of *Freedman v Freedman & Others*, Mr Freedman settled money on his daughter (not for any tax purpose, but for purely personal and family reasons) having been advised that no inheritance tax liability would arise because of the life interest of his daughter. Unfortunately, the advice had overlooked that since 2006 such a gift would be a lifetime chargeable transfer giving rise to an immediate 20% charge. This had such a serious effect on the family's financial situation and their relationships that the High Court thought this was properly described as grave. The large tax liability which arose was extremely serious and the court decided it would be unconscionable for others to profit from this mistake and the settlement was accordingly set aside on the grounds of equitable mistake.

This does not break new ground, but confirms the principles established by the Supreme Court in *Pitt* which are life-saving in the right circumstances. HMRC opposed the application, not it seems out of any particular wish to disadvantage the applicant, but just to ensure that all the relevant arguments were fully articulated before the court. **NLJ**

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