Briefing

Private client review for September

Speed read

This month, we report on forthcoming changes to the CGT rules on transfers of property between separating spouses and civil partners. *Jenner* provides a useful reminder that any information requested by HMRC in an information notice must be 'reasonably required' to check the taxpayer's tax position. In *Firth*, the taxpayers fail to persuade the FTT that their interest in an 'aparthotel' business qualified for BPR. The UT also clarifies, in *Priory London Ltd and Jocoguma Properties Ltd*, that notices of daily penalties for the late filing of ATED returns can be issued retrospectively. Finally, we comment on the launch of the new register of overseas entities and its interaction with the Trust Registration Service.

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Relaxation of CGT rules on separation and divorce

It is well known that spouses or civil partners are able to transfer assets freely between each other without triggering an immediate CGT charge on the disposal of the asset (known as a 'no gain no loss' transfer). However, couples who are separating or divorcing can be caught out by existing rules which extend this treatment only for the remainder of the tax year in which they separate. Transfers made from the following tax year are deemed to take place at market value and taxed accordingly.

In a May 2021 report on CGT, the Office of Tax Simplification (OTS) noted that 'it is unrealistic to expect separating couples to have resolved their affairs by the end of the tax year of their separation' and recommended that the window for no gain no loss transfers be extended to allow separating couples at least two tax years after the separation event to make transfers, or an even longer period provided it is reasonable and in accordance with a financial agreement approved by a court.

On 20 July, the government published draft legislation for the Finance Bill 2022/23 which amends the CGT rules for transfers of property between separating spouses and civil partners.

The draft legislation is more generous than the OTS's recommendations. Under new rules, applying to disposals made on or after 6 April 2023, separating spouses or civil partners will be able to continue to make transfers between each other on a no gain no loss basis for:

- up to three tax years after the tax year in which the couple cease to live together; or
- an unlimited period where the transfers are made in accordance with a formal divorce agreement or court order.

There will also be special rules introduced for individuals who maintain a financial interest in their former family home following separation, including the ability for the non-occupying former spouse or civil partner to claim principal private residence relief on a future sale of the property.

This is positive news for divorcing couples, giving them more time to reach an agreement on the division of their assets without running the risk of an unwelcome tax bill adding to the stress of separation.

Information notices and HMRC fishing expeditions

FA 2008 Sch 36 para 1(1) provides that HMRC may 'require a person ('the taxpayer') (a) to provide information, or (b) to produce a document, if the information or document is reasonably required by the officer for the purpose of checking the taxpayer's tax position.'

The recent First-tier Tribunal (FTT) decision of *Jenner v HMRC* [2022] UKFTT 203 (TC) considered what is meant by 'reasonably required' in this context.

Mr Jenner submitted tax returns for the 2016/17 and 2017/18 tax years, disclosing self-employment turnover of £1 for each year and foreign income of £194 for the first year and £2,316 for the following year. HMRC then opened enquiries into both returns and issued information notices on the basis that Mr Jenner's declared income did not appear to be sufficient to meet his cost of living and personal expenditure 'by a significant margin.'

> The FTT considered that a taxpayer 'should not be required to divulge details of his personal expenditure if that could be avoided'

The information notices requested information and documents in three categories:

- household expenditure – asking for details of Mr Jenner's rent, utilities bills, food costs, and the dates and cost of any holidays;
- financial information – seeking an analysis of any director's loan accounts and amounts drawn from trusts, partnerships or other individuals; and
- personal accounts – requesting a schedule detailing all of Mr Jenner's personal financial accounts, together with statements for the accounts.

It was accepted that the burden of proof rested on HMRC to show that the information requested was 'reasonably required'. The FTT noted that 'HMRC are not permitted to make broad requests for the purposes of fishing for information' as this 'would not meet the "reasonably required" test'. However, that did not mean that they needed to have suspicions in order to check a tax return.

The FTT considered that the information requested in the second and third categories amounted to 'basic financial information' which is reasonably required by HMRC in order to check Mr Jenner's tax position. Accordingly, even though the FTT accepted that HMRC may have been able to obtain some of this information from other sources, it was reasonable for HMRC to require Mr Jenner to provide it in these circumstances, and so upheld these requests (subject to a minor variation).

However, in relation to the first category (details of household expenditure), the FTT considered that a taxpayer 'should not be required to divulge details of his personal expenditure if that could be avoided', concluding that this broad request did not meet the reasonably required test and should be set aside.

We have previously commented in this column on the limits to HMRC's powers to demand information. This case serves as a further reminder to taxpayers and their advisers to consider, when served with an information notice, whether the information requested is 'reasonably required' or whether HMRC are on a fishing expedition.

Business property relief: aparthotel business fails to qualify

Business property relief (BPR) is a valuable tax relief, allowing taxpayers to claim inheritance tax relief on 'relevant business property'. However, business interests or shares in a company do not qualify as 'relevant business property' if the business consists wholly or mainly of holding investments.

There have been a number of decisions looking at the availability of BPR in the context of businesses which provide accommodation, in particular, furnished holiday lets. Most recently, the FTT considered whether the taxpayers' interest in an 'aparthotel' business qualified for BPR in *Firth v HMRC* [2022] UKFTT 219 (TC).

The taxpayers argued that the business was comparable to a boutique hotel, whereas HMRC submitted that it was the equivalent of a furnished holiday letting. The Tribunal took into account a variety of factors in determining whether the business' non-investment activities were more significant than its investment activity of holding land. Non-investment activities included the provision of a welcome pack to guests, cleaning services if requested, linen, shower gel, furniture, white goods, DVD players/TVs, Wi-Fi, food and the ability to purchase extra packages such as flowers, chocolates, birthday cakes and prosecco. However, other activities (such as marketing, benchmarking letting rates, preparing the apartments for guests, dealing with complaints and requests, maintenance and repairs of the properties) were all categorised as investment activities, designed to maximise the taxpayers' return from their investment in the properties themselves.

The FTT concluded that, although some aparthotels could be categorised as a service business with an ancillary investment in land, on the facts of this case, the non-investment activities of the business were ancillary to the investment in land. Accordingly, the taxpayers' interest in the business was not 'relevant business property' and so did not qualify for BPR.

BPR is estimated to cost the exchequer over £1bn each year, and possible reforms to the relief have been discussed at length in recent years. Various proposals were made by the OTS in July 2019 – some of these suggestions would have resulted in a tightening up of the relief but a specific recommendation was made 'to align the Inheritance Tax treatment of furnished holiday lets with that of Income Tax and Capital Gains Tax, where they are treated as trading providing that certain conditions are met'. However, the government confirmed at the end of 2021 that it has no current plans to proceed with any changes.

All of these cases turn on the facts, but advisers should remain aware of the factors that the court will consider in determining whether a business' investment activities are ancillary or not.

ATED: clearing up confusion: notice of daily penalties *can* be issued retrospectively

In *Priory London Ltd v HMRC* and *HMRC v Jocoguma Properties Ltd* [2022] UKUT 225 (TCC) (heard together), the Upper Tribunal (UT) held that notices of daily penalties for the late filing of ATED returns can be issued retrospectively, clarifying a previously uncertain position.

The two appeals were heard separately by the FTT, where different conclusions were reached. In both cases, the companies filed late ATED returns, triggering an initial fixed penalty of £100 from HMRC. In the penalty notices, HMRC said that daily penalties would be charged if the returns were made over three months late (under FA 2009 Sch 55 para 4). HMRC then charged the maximum daily penalties, along with additional fixed penalties, relating to periods prior to the original penalty notice date. Both companies appealed.

The legislation (para 4(1)(c)) requires penalty notices to specify the date from which penalties for late filing are payable and provides that the applicable penalty date may be earlier than that on which notice is given (para 4(3)). This is important in the context of the ATED regime, where HMRC may be unaware that a return is due until it is submitted.

> Whilst this Upper Tribunal decision may not be welcomed by taxpayers, it at least brings clarity to a previously ambiguous position.

The FTT in both cases considered the timing of notices in *Advantage Business Finance Ltd* [2019] UKFTT 30 (ABF) and *Heacham Holidays Ltd v HMRC* [2020] UKFTT 406 (following *HMRC v Donaldson* [2016] EWCA Civ 761). These found that para 4(1)(c)'s purpose was to warn taxpayers of their potential liability to daily penalties. Meaning that, on a purposive construction, a notice could not be given retrospectively. In *Jocoguma*, the FTT followed these decisions, whereas in *Priory* the FTT held that a notice could be issued retrospectively. This was evidently an unsatisfactory position.

The UT decided that *ABF* and *Heacham* were incorrectly reasoned. *Donaldson* (which was an income tax case involving circumstances in which HMRC would have had advance notice of the requirement to file a return) and para 4(1)(c) should be read to conclude that warning taxpayers of potential daily penalties was only one of the notices' purposes. Notices could therefore be issued retrospectively in all cases (rather than just exceptionally). On this basis, the UT dismissed the *Priory* appeal and allowed HMRC's appeal against the FTT's decision in *Jocoguma*.

Whilst this decision may not be welcomed by taxpayers (who may otherwise have an argument that they are protected from penalties by omitting to file returns), it at least brings clarity to a previously ambiguous position.

A new era for transparency: launch of the ROE and enforcement of the expanded TRS regime

Readers will no doubt be aware that the new register of overseas entities (ROE) which hold UK land was launched on 1 August (see our April review in *Tax Journal*, 15 April 2022).

Under this, an overseas entity that holds or acquires UK land will need to register with Companies House and provide details of its 'beneficial owners'. If a beneficial owner is a trustee, information about the trust must also be provided. Much of the information will be publicly available (although trust information will only be available to tax authorities).

Broadly, an overseas entity holding UK land since 1 January 1999 and pre-1 August 2022 must register by 31 January 2023. From 5 September 2022, overseas entities that wish to register UK land acquisitions with HM Land Registry are unable to do so without first being registered on the ROE.

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An overseas entity cannot apply for registration unless a 'relevant person' (for example, a lawyer or accountant) first verifies the registration information (and the verifier must also first register with Companies House). The Law Society has urged the legal profession to exercise extreme caution in acting as a verifier, warning of the risks, including potential criminal liability, if the necessary standards are not met. It remains to be seen how this will play out, with the majority of law firms currently not offering these services.

Notably, the ROE is a separate regime to other transparency initiatives, including the Trust Registration Service (TRS). It may therefore be that the same trust needs to register under both regimes (for example, where a non-UK resident corporate trustee purchases UK land directly, the corporate must register as an overseas entity on the ROE and the trust will need to register with the TRS).

For the TRS, 1 September marked the deadline by which trusts falling within the expanded scope of the regime must register. HMRC has clarified that there will be no penalty for a first offence of failure to register or late registration provided the omission was not due to deliberate behaviour by the trustees. This will no doubt be welcome news, particularly given recent HMRC figures, indicating that approximately one million trusts still need to register. However, this should not prompt relaxation, as the position may well change as the regime becomes more established and, where HMRC considers failure to be deliberate, they may impose a fine of £5,000 per trust. ■

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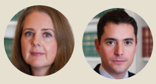

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