

Entrepreneurs' relief and life interest trusts

(Lecture P1169 – 12.45 minutes)

If a business asset such as a shareholding in a family trading company is held in a discretionary or accumulation trust, a subsequent sale of those shares by the trustees can never qualify for entrepreneurs' relief. The trustees' CGT will always be at the rate of 20% (or 28% for tax years prior to 2016/17).

However, the sale of shares held in a life interest trust where there is a 'qualifying beneficiary' (as defined in S169J(3) TCGA 1992) can attract this valuable relief provided that the life tenant is prepared to surrender all or part of his personal entrepreneurs' relief entitlement, in which case the 10% rate will be in point.

In order for there to be a 'qualifying beneficiary' where a pre-FA 2019 sale of shares is concerned, three separate conditions set out in S169J(4) TCGA 1992 must be satisfied throughout a period of 12 months ended in the three years up to the date of the trustees' disposal:

- the company to which the shares relate must have been a trading company or the holding company of a trading group;
- the life tenant must have been an officer or employee of the company (or, where the company is a member of a group, of any other member of its group); and
- the life tenant must have personally held at least 5% of the company's ordinary share capital and voting rights.

It should be noted that there is no requirement for the trustees themselves to pass the 5% test.

Where the requirements above are satisfied and where the life tenant is willing to assign the benefit of all or part of his lifetime entrepreneurs' relief limit to the trustees, they can claim entrepreneurs' relief of up to £10,000,000 and the trust gain will only be chargeable at 10%.

As a result of what has always been assumed to be an oversight, there is no rule in TCGA 1992 which states that the life tenant must have been a 'qualifying beneficiary' for at least a 12-month period. Thus it has been possible for, say, a discretionary trust to 'parachute in' a suitable beneficiary as a life tenant for a short period, during which time the shares are sold. Because the trust (or the relevant part of it) has been converted to a life interest one, it now meets the conditions set out in S169J TCGA 1992 and so an appropriate claim can be made. If the life interest is subsequently revoked, this does not cause the claim to fail.

At a meeting of the Capital Taxes Liaison Group in 2017, the minutes of which were published by the CIOT on 19 September 2018, HMRC indicated that, in their opinion, such a planning ploy did not work. This followed, they said, from the words of the statute which is written in terms of a 'qualifying beneficiary', and not simply of an individual. Interestingly, HMRC have previously given advice with contradicted this standpoint. However, they were saying in 2017 that the technical adviser who had provided that guidance was wrong.

A senior HMRC official confirmed that he had asked his technical colleagues to withdraw the advice and clarify the situation, but there was no mention of the fact that, if and when they did that, it would surely be necessary for HMRC to specify an effective date from which the corrected interpretation would apply to trust disposals.

In the event, this may all prove to have been unnecessary. On 6 August 2019, the First-Tier Tribunal published Judge Guy Brannan's unequivocal decision in *The Quentin Skinner 2005 Settlements v HMRC (2019)*, in which he categorically stated that the relevant part of TCGA 1992 did not have the meaning contended by HMRC.

The facts of this case were as follows:

- Three beneficiaries had been given life interests in three settlements on 30 July 2015 and then on 11 August 2015, shares in a trading company called DPAS Ltd were transferred to the settlements.
- DPAS Ltd had been the personal company of each of the three beneficiaries since 2011 under the pre-FA 2019 definition of this term in S169S(3) TCGA 1992.
- Each of the three beneficiaries was an officer of DPAS Ltd.
- On 1 December 2015, the trustees disposed of the shares in DPAS Ltd.
- On 31 January 2017, the trustees (together with each of the three beneficiaries) made claims for entrepreneurs' relief in accordance with the provisions set out in S169M TCGA 1992.

Although HMRC refused leave to make such claims, this rejection has been overturned by the First-Tier Tribunal. It will be interesting to see whether HMRC seek to take this case to the Upper Tribunal. Either way, a change in the wording of the statute is likely.

Contributed by Robert Jamieson