

‘Just and reasonable’ or not? (Lecture P1257 – 10.59 minutes)

In FA 2008, the previous taper relief regime for CGT was replaced by entrepreneurs’ relief (now renamed business asset disposal relief). One of the key differences between the tax treatment for the two types of relief was where, over a period of ownership, property such as a shareholding was classified as both a qualifying and a non-qualifying asset.

Under taper, there were two categories of relief:

1. business asset taper relief (BATR); and
2. non-business asset taper relief (non-BATR),

with the former attracting a more generous deduction than the latter. If an asset was entitled to receive both BATR and non-BATR over its holding period, any gain on a disposal had to be split between the two components. One part of the gain was reduced by BATR, while the other part was reduced by the less advantageous non-BATR.

The legislation for business asset disposal relief has a completely different *modus operandi*. Provided that an asset qualifies over a requisite period (which nowadays represents the last two years of ownership), business asset disposal relief is available. This involves the application of a special 10% CGT rate to the gain. However, if the relevant requirements are not met, there is no relief and the normal rate of CGT is in point (which, in most cases, will be 20%).

It should be appreciated that the present system offers better tax planning possibilities. If an asset such as shares in an unlisted trading company does not currently attract business asset disposal relief (perhaps because the owner is not an officer or employee), it may be a relatively straightforward matter to put this right. If the requisite waiting period is then satisfied, full relief is available on an unrestricted basis when the shares are sold, despite the fact that they may have previously had non-qualifying status for several years. This contrasts with the taper relief rules described above.

The Upper Tribunal decision in *Lee v HMRC* (2020) had to consider the mechanism for splitting gains where both BATR and non-BATR applied. The taper relief provisions, which are of course no longer with us, were found in Sch A1 TCGA 1992. Of particular relevance were:

- Para 3 Sch A1 TCGA 1992; and
- Para 21 Sch A1 TCGA 1992.

Para 3 Sch A1 TCGA 1992 set out the basic approach to be adopted where BATR and non-BATR were applicable. The gain on the asset’s disposal had notionally to be divided into a business asset gain and a non-business asset gain in proportion to the periods during which the asset was, and was not, a business asset. The appropriate taper relief percentages were then applied to the respective part gains as if those gains had arisen on separate assets held throughout the overall period of ownership. In other words, straight-line time-apportionment was the name of the game.

If Para 21 Sch A1 TCGA 1992 applied, the division had to be done on a ‘just and reasonable’ basis. However, this phrase was not defined in the legislation and HMRC’s Capital Gains Manual provided no real guidance on how such an apportionment should be effected.

The question which the Lee case had to determine was: which of these two provisions took precedence?

In this dispute, the taxpayer (L) disposed of a shareholding on 12 March 2003 which was classed as a non-business asset from 6 April 1998 (when taper relief started) up to 5 April 2000 but as a business asset from 6 April 2000 up to 12 March 2003. L argued that most of his gain should be attributed to the second period which attracted a much more favourable deduction on the ground that there had been what the case report calls 'a dramatic increase in the value of the shares after April 2000'. L was invoking the 'just and reasonable' principle.

HMRC, on the other hand, contended that the statutory rule in Para 3 Sch A1 TCGA 1992 was essentially prescriptive. That is to say, a time-based formula had to apply.

The Upper Tribunal agreed with HMRC's reasoning. The judges said that the only circumstances in which Para 21 Sch A1 TCGA 1992 would be relevant were where there had to be an allocation because, for example, an asset used in a seasonal business would not, by definition, be used through the whole tax year. But these situations would be very limited. Effectively, therefore, Para 3 Sch A1 TCGA 1992 ruled the roost.

The judges also pointed out that any other interpretation would mean that Para 3 Sch A1 TCGA 1992 could almost always be overridden since it was very unlikely in practice that a gain would arise on an absolute straight-line basis over time.

L lost his case. Although taper relief was abolished as long ago as 2008 so that there are unlikely to be further cases coming before the Tribunals on this point, it should not be overlooked that there are other instances in the CGT code where there is a time-apportionment rule and so the Lee decision could still be significant.

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