

## **A CGT trust uncertainty resolved (Lecture P1344 minutes – 24.46 minutes)**

The Court of Appeal's decision in *The Quentin Skinner 2015 Settlements v HMRC* (2022) examines the relationship between entrepreneurs' relief and the disposal of shares in a qualifying trading company held in an interest in possession trust. Subsequent to the events in the case, entrepreneurs' relief has been renamed business asset disposal relief, but the findings of Sir Launcelot Henderson and his two fellow judges would be unaffected by this change.

If an asset such as a shareholding in a family trading company is held in a discretionary or accumulation trust, a sale of those shares by the trustees can never qualify for entrepreneurs' relief or business asset disposal relief. The trustees' CGT will always be at the full 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 so that the 10% tax rate will be in point. This is subject to the caveat that the life tenant is prepared to surrender the relevant part of his personal relief entitlement to the trustees.

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 one year 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.

Note 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 the relevant part of his lifetime limit to the trustees, the trustees can claim relief of up to (currently) £1,000,000 so that their 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 one-year period. Thus, it was 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 has been converted to a life interest one, it meets the conditions set out in S169J TCGA 1992. As a result, an appropriate claim can be made. If the life interest is subsequently revoked, it is argued that 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 would 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 had previously given advice which contradicted this standpoint.

However, they were now arguing 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.

With hindsight, this official position has been shown to be incorrect. The Court of Appeal refuted HMRC's contention that relief was not available. In doing so, the judges backed up the decision of the First Tier Tribunal which was given in 2019.

### *Case facts*

Three settlements were made on 30 July 2015. The principal beneficiary of each settlement was one of the settlor's three sons.

The initial settled property was £10 per trust, but, on 11 August 2015, the settlor gave 55,000 'D' ordinary shares in a trading company called DPAS Ltd to the trustees of each settlement. The business of this company involved the administration of insurance services for dentists.

Because each beneficiary had a present right of present enjoyment of the income from the DPAS Ltd shares, they had an interest in possession in the trust assets (see *Pearson v CIR* (1980) which was a decision on the meaning of 'interest in possession' for the purposes of CTT (later IHT), but, per Sir Launcelot Henderson, no-one has suggested that this expression should have a different meaning for the purposes of CGT).

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. They had each owned 32,250 'C' shares in the same company, and it was common ground that such a holding was sufficient to make DPAS Ltd the personal company of the three beneficiaries.

Each of the three beneficiaries was an officer of DPAS Ltd.

On 1 December 2015, the trustees disposed of the shares in DPAS Ltd (i.e., less than four months after they acquired them).

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.

The Court of Appeal agreed that it was only necessary for the three key ingredients in S169J (1) TCGA 1992 to be present throughout the requisite one-year period. Nowhere does it say that the beneficiary's interest in possession must be in place on the date of the disposal and throughout the above one-year period. In Sir Launcelot Henderson's words:

'It would in my judgment be wholly foreign to this carefully delineated statutory scheme if the reader then had to extract from S169J(4) and (5) TCGA 1992 a further condition, nowhere expressly articulated and conspicuously absent from S169J(3) TCGA 1992 itself, to the effect that the qualifying beneficiary's interest in possession must subsist not only on the date of disposal but also throughout the one-year period when the "relevant condition" is met.

If that had indeed been the statutory intention, one would expect the additional requirement to have been expressly included in the definition of a qualifying beneficiary.'

Given that this was not the case, it was logical to conclude that HMRC's arguments were misconceived. The trustees won their case and, in doing so, apparently saved CGT of some £1,750,000. Remember that, in 2015/16, the entrepreneurs' relief cap was £10,000,000 and the main CGT rate accruing to the trustees of a settlement was 28%.

Those advising on business asset disposal relief and trusts should study this decision with care. Indeed, anyone with an interest in how the Courts interpret difficult pieces of legislation will find plenty here to interest them. Sir Launcelot Henderson's comments about the drafting techniques used as a result of the Tax Law Rewrite Project are particularly worth reading.

*Contributed by Robert Jamieson*