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Motivational speaking

A trustee's guide to the UK's income and capital gains tax motive defences

Transfer of Assets Abroad



- Anti-avoidance provisions
 - Ss720 - 735 Income Tax Act 2007
 - S.3 Taxation of Chargeable Gains Act 1992
- Aim to counter and discourage the use of offshore structures as a means to avoid UK tax by imposing an income tax or capital gains tax charge on a transferor to or beneficiary of a structure if certain criteria are met

Income tax motive defence

“the application of the motive defence in any particular case will always be a matter for determination on the facts by the tribunal”



- Income tax ToAA provisions impose an income tax charge where a UK resident person:
 - Has the power to enjoy income arising to a person abroad because of relevant transfers and/or associated operations (ss.720 -726) (the "**transferor power to enjoy income**")
 - Receives capital sums connected to a relevant transfer and, as a result of relevant transfers and/or associated operations, income arises to a person abroad (ss.727 – 730) (the "**transferor capital sum rules**"); or
 - Receives a benefit out of assets available for the purpose because of a relevant transfer and/or associated operations (ss.731 – 735) (the "**beneficiary provisions**")



- Where ToAA provisions apply:
 - If the transferor provisions are engaged - income arising within the structure is taxed on the transferor as if it arose to the transferor directly
 - If the beneficiary provisions are engaged – “relevant income” within the structure is matched against the benefit received
- 2017 changes
 - Protected trusts regime - switches off transferor provisions for foreign source income in some circumstances
 - Persons who were previously “transferors” may now fall within the beneficiary rules if they are able to benefit from the structure

Income tax motive defence

Introduction

Or motive defences... (thanks Mr Brown!)

Key weapon in the armoury to protect structures which had no UK nexus on creation but now have a link to the UK (e.g. a UK resident beneficiary)

In principle – if the purpose behind the transactions/structuring is not tax avoidance then the MD should protect the transferor/beneficiary.



Income tax motive defence

Specifics



- HOWEVER it's not as easy as that!
- **Condition A**
 - It would not be reasonable to draw the conclusion from all the circumstances of the case that the purpose of avoiding a liability to taxation was the purpose, or one of the purposes, for which the relevant transactions or any of them were effected.
- If not condition A, then **Condition B**
 - all of the relevant transactions were genuine commercial transactions; and
 - it would not be reasonable to draw the conclusion, from all the circumstances of the case, that any one or more of the transactions was more than incidentally designed for the purpose of avoiding liability to tax

Income tax motive defence



- Test is subjective
- Look at individual's circumstances and reactions, not just what they say their purpose is
- Purpose requires knowledge

Tax avoidance?

"The concept of avoidance is a slippery one"

What is the purpose?



- Avoiding the liability to tax only needs to be a purpose
- Looks at purpose of the transfer not the transferor
- Condition A – requires no tax avoidance purpose at all for the relevant transactions
- Condition B – requires that the transactions were not designed for the purpose of avoidance

What is avoidance?



- Avoidance takes its technical meaning: "a course of action designed to conflict with or defeat the evident intention of parliament" (*IRC v Willoughby* 70 TC 57)
- Can include deferral of tax
- How much can tax be a motivation? A tax avoidance effect does not prevent motive test applying

What is not avoidance?



- Knowledge that less tax is paid
- Awareness of tax aspects
- Taking tax advice
- Picking a lower tax route over a higher tax route

What is tax?



- Tax is very widely drawn and covers “any revenue for whose collection HMRC is responsible”
- Not just income tax...
- *Fisher v HMRC* concluded that it covered betting duty and no purpose to avoid IT required (HMRC’s draft guidance needs to change!)

EU motive defence

EU motive defence



- Post 5 April 2012 transactions where ss.720 to 735 ITA 2007 would apply
- **Condition A** - viewed objectively the transaction would be considered genuine and, were the individual to be liable to tax, that liability to tax would constitute an "unjustified and disproportionate restriction" on the freedom protected by a relevant treaty provision, in contravention of that treaty provision
- **Condition B** – the transaction is a genuine transaction (viewed objectively)
- Still relevant despite Brexit – but for how much longer?

Case update

(But watch this space.....)

Points from recent cases



- Two recent UTT decisions on ToAA both determined no liability on basis outside scope of the provisions – i.e. motive defence wasn't needed
- Key concept of who is 'transferor' – need to look at who is the "real transferor"
 - In exceptional case includes person who "procures" the transfer
 - Not enough to "have a hand in" or be "associated with" the transfer
 - Shareholders/directors of a company cannot have the transfers of the company attributed to them (& no mechanism in the legislation to ascribe a % to a shareholder)

Rialas v HMRC



- Mr R only transferred initial £10 to trust to subscribe for shares in underlying company
- Balance of funds was borrowed (\$15m) and used to acquire shares
- This was held to not fall within “associated operations”
- FTT held that using non-resident trust to hold UK shares had a motive to avoid inheritance tax & therefore the IT motive defence was not available



- Quantum of the charge: profits of new business ventures were “associated operations” as only possible due to income generated by assets original transferred
- Condition B motive defence would be available as genuine commercial transactions and transaction was not designed with purpose of avoiding betting duty
- EU motive defence not applicable between UK and Gibraltar (but extended to allow Stephen to benefit from Anne’s exercise of her freedom of establishment)

CGT motive defence

CGT anti avoidance



- S.3 TCGA 1992 (was s.13)
- Chargeable gain accrues to a company that would be close if it were in the UK (i.e. controlled by five or fewer participators or any number of participators who are directors)
- Gain is "connected to avoidance"
- Gain is not connected to foreign trade or other economically significant activity
- Apart from s.3, some or all of the gain would not be subject to corporation tax

If CGT anti-avoidance applies...



- Gain accruing is apportioned to participators
- UK resident participators are taxed as if they realised the gain directly
- Non-UK resident trustees add the gain to the s.87 gains pool, ready to be matched on a later distribution to a UK resident beneficiary
- Catches direct and indirect participators
- 25% rule



- Younger than the IT motive defence – only added to the statute book in 2013

When is a gain not “connected to avoidance”?

- Negative test. Disposal of an asset by the company will be taken to be connected to avoidance unless neither:
 - The disposal of the asset by the company; nor
 - The acquisition or holding of the asset by the company in the first place

formed part of a scheme or arrangements the main purpose or one of the main purposes was the avoidance of liability to CGT or corporation tax



- Only CGT or corporation tax (on chargeable gains) avoidance matters
- Avoidance tested as for income tax motive defence

Schemes and arrangements

- Can take place over a long period of time but still constitute a single settlement arrangement
- Whole scenario doesn't need to be in contemplation from the outset but there must be "sufficient unity"

Easier to prove?



- Possibly
- Statutory rebase indicates that parliament would have accepted the motive defence for those structures

Motive defence in practice

Is a claim required?



- Need to include notification that have applied IT motive defence in tax return and provide:
 - 'amount omitted' and
 - 'full details' - details of the assets transferred, any associated operations, the person abroad concerned, the circumstances of the relevant transactions and the basis of the claim
- Disclosure protects from discovery assessment if the motive defence is reconsidered in later years (RI201)
- No such requirement for CGT motive defence

Record keeping is important!



To determine the purpose(s) for which the relevant transaction(s) were effected, statute requires that we look at the intentions and purposes of the person who (i) designs or effects or (ii) provides advice in relation to the transactions or any of them. (Income tax motive defence)

Our documentation could have vital importance.

If a person relies on professional advisers and executes documents with no more than a vague idea of approving proposals put to them, they have adopted the purpose of their advisers or (which comes to the same thing) the purpose of their advisers should be attributed to them. James Kessler

You have been watching:



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