

## AAT tax update 31 May 2015

In this edition of the tax update we look at:

1. Further clarification on the Courts rectifying a mistake in a contract
2. New Treasury team and a budget on 8 July 2015
3. No appeal against FTT decision on FA 2008, Schedule 36 taxpayer notice
4. HMRC 2015/16 guidance on PAYE (CWG2)

### 1. Further clarification on the Courts rectifying a mistake in a contract

In the March edition of the tax update I had reviewed and summarised *Joost Lobblert* which was a case of a man ticking the wrong box with the result that the premature encashment of Life Assurance policies created a significant tax liability when the commercial reality was that he had made a loss. It was a just decision and I criticised HMRC for pursuing the appeal when the outcome was so unjust that no reasonable person should have objected to what was obviously remedying a mistake.

What I might describe as the *Hastings Bass principle* was restricted considerably by some recent decisions, including the Supreme Court's decision in *Pitt v. Holt, Futter v. Futter* [2013] UKSC 26; [2013] 2 AC 108. If I might paraphrase these decisions, the Supreme Court was making it clear that it would be unsympathetic to remedying any contracts which were entered into for the purposes of tax avoidance, and it was not the Court's function to protect indemnity insurers. If professional advice had been obtained and that advice was wrong, the recourse was to seek compensation from the adviser and not to amend the contract.

In *Kennedy v. Kennedy* [2014] EWHC 4129 (Ch) Etherton C summarised the principles applicable to rescission of a non-contractual voluntary disposition for mistake as follows (at [36]),

- “ (1) There must be a distinct mistake as distinguished from mere ignorance or inadvertence or what unjust enrichment scholars call a "misprediction" relating to some possible future event. On the other hand, forgetfulness, inadvertence or ignorance can lead to a false belief or assumption which the court will recognise as a legally relevant mistake. Accordingly, although mere ignorance, even if causative, is insufficient to found the cause of action, the court, in carrying out its task of finding the facts, should not shrink from drawing the inference of conscious belief or tacit assumption when there is evidence to support such an inference.
- (2) A mistake may still be a relevant mistake even if it was due to carelessness on the part of the person making the voluntary disposition, unless the circumstances are such as to show that he or she deliberately ran the risk, or must be taken to have run the risk, of being wrong.
- (3) The causative mistake must be sufficiently grave as to make it unconscionable on the part of the donee to retain the property. That test will normally be satisfied only when there is a mistake either as to the legal character or nature of a transaction or as to some matter of fact or law which is basic to the transaction. The gravity of the mistake must be assessed by a close examination of the facts, including the circumstances of the mistake and its consequences for the person who made the vitiated disposition.
- (4) The injustice (or unfairness or unconscionableness) of leaving a mistaken disposition uncorrected must be evaluated objectively but with an intense focus on the facts of the particular case. The court must consider in the round the existence of a distinct mistake, its degree of centrality to the transaction in question and the seriousness of its consequences, and make an evaluative judgment whether it would be unconscionable, or unjust, to leave the mistake uncorrected.”

In *Freedman v Freedman & Ors* [2015] EWHC 1457, an interest in possession trust had been created to hold property occupied by Melanie Freedman on the advice of her father, Charles Freedman (who died on 27 June 2013), and Mr Peter David Fraser, a solicitor with OGR

Stock Denton LLP. Melanie is now aged 53. The property subject to the settlement solely comprises two houses, which I shall respectively call "St Leonard's Close" and "Gibbs Green".

In 2001 her father helped Melanie buy St Leonard's Close for her to live in with her son. Her father lent her the price of £279,950 and all of the costs of purchase subject to a charge on St Leonard's Close. In about 2004 to 2005, when her relationship with Mr Bakir had ended, her father agreed to forgo the loan, and the charge was removed. Then in about April 2010 Melanie left St Leonard's Close to be closer to her son's school, where she worked as a dinner lady. She let St Leonard's Close and moved into rented accommodation. She found Gibbs Green but had difficulty selling St Leonard's Close. The unchallenged evidence is that Melanie has very little money and very little earning power. By contrast, her father was a rich man as his inheritance tax account shows. Melanie again approached her father who agreed to lend her the purchase price (£525,000) for Gibbs Green and the acquisition costs of £5,000.

It seems that Ms Freedman's father was concerned that she might be adversely affected by predatory men and he suggested placing the properties into a trust. Ms Freedman did not consider that such a step might have taxation consequences or other disadvantages. She relied on her father and Messrs OGR Stock Denton, the solicitors he engaged to protect her interests. Every reader will have alarm bells ringing that the properties cost over £800,000 and the transfer into a trust would be a lifetime chargeable transfer creating an IHT liability. Not to mention the rental income in the trust becoming liable to higher rates. The amount of the tax charged on entering into the settlement was some £156,000 (plus interest),

The solicitor, Mr Fraser, failed to appreciate the effect of s. 49(1A) of the Inheritance Tax Act 1984 ("IHTA") on interests in possession to which a person becomes entitled on or after 22 March 2006, and advised Melanie's father that the full value of the settled property remained part of Melanie's estate. He admits (at [16] of his witness statement) that he failed to realise, and thus explain, that the transfer of assets into the trust would be a lifetime chargeable transfer for inheritance tax purposes and (to the extent that the net value exceeded the nil rate band) there would be an immediate entry charge of 20%. He also admits that he failed to realise or explain that there would be a 10-yearly charge and (counter to the intention that the proceeds of St Leonard's Close would be appointed to Melanie to pay off the loan from her father) exit charges.

The Court was being asked to make an order under Part 8 to set aside the settlement on the grounds of equitable mistake. In order for relief to be given, there must be a distinct mistake, a serious mistake, and it must be unconscionable not to set the settlement aside. In addition, it is likely that relief will not be given if the transaction is part of a tax avoidance scheme.

All the family members supported the application. The only objector was HMRC. The Court granted relief under Part 8 and set aside the settlement on the grounds of equitable mistake. The position is that Melanie has made a distinct and serious mistake. The settlement was not created for the benefit of the beneficiaries, but to protect Melanie. If the settlement remained, Melanie has a large tax liability which affects her ability to repay the loan which she took on the basis that it would be repaid. Taking the matter in the round, it would be unconscionable for the donees to profit from that mistake and insist on their rights under the settlement.

<http://www.bailii.org/ew/cases/EWHC/Ch/2015/1457.html>

## **2. New Treasury team and a budget on 8 July 2015**

The Treasury team has been confirmed as follows:

First Secretary of State & Chancellor of the Exchequer – Rt Hon George Osborne MP  
Chief Secretary to the Treasury – Rt Hon Greg Hands MP  
Financial Secretary to the Treasury – David Gauke MP  
Exchequer Secretary to the Treasury – Damian Hinds MP  
Economic Secretary to the Treasury – Harriett Baldwin MP

You can read about all of the ministerial appointments confirmed on 14 May 2015 [here](#).

The next budget will be on 8 July 2015.

### **3. No appeal against FTT decision on FA 2008, Schedule 36 taxpayer notice**

There is a difficult balance to be struck between the right of the state to obtain information which is reasonably required to check the accuracy of a tax return, and the rights of privacy which should be respected. Over the years I have seen many examples of HMRC seeking information which was irrelevant to any tax liability. As a general rule, objecting to the information notice produced the desired result and when the case was reviewed by a more experienced and senior officer, the unreasonable requests would be dropped.

However it is reasonable for HMRC to have powers which enable them to check business records and to inspect business premises. In *Carmel Jordan –v- HMRC* [2015] UKUT 0218, the taxpayer, a taxi driver, had objected to a business records check and the appeal had been heard by the First Tier Tribunal (FTT). The FTT concluded that the notice was valid in principle, but allowed the appeal in part by removing four items from the list of required documents and information, they said duplicated other items, and by removing one further item which they said was not reasonably requested. Importantly, they confirmed the view that there is no right of appeal against a request for business records.

A decision of the FTT on an information notice is final and the Upper Tribunal had no jurisdiction to hear a further appeal. The UT struck out the appeal confirming that HMRC had a right to access statutory records which are reasonably required to check the taxpayer's position and returns.

<http://www.tribunals.gov.uk/financeandtax/Documents/decisions/Carmel-Jordan-v-HMRC.pdf>

### **4. HMRC publish 2015/16 guidance on PAYE (CWG2)**

HMRC have published the latest essential reading for employers and advisers on operating PAYE for tax and National Insurance contributions. It highlights the rules for day to day operation of RTI PAYE and special rules, for example, employee share and option schemes, for payments around Bank Holidays and for harvest workers and shoots.

<https://www.gov.uk/government/publications/cwg2-further-guide-to-payee-and-national-insurance-contributions>

Derek Allen  
31 May 2015

Set your diaries for the next edition of the general tax update which will be published at the end of June 2015

The views expressed in these podcasts are Derek Allen's personal views and do not necessarily represent AAT policy or strategy.