[2017] UKUT 0111 (TCC)

Appeal number: UT/2014/0071

INCOME TAX AND CAPITAL GAINS TAX – whether claims for relief in relation to assets that became of negligible value and loans that became irrecoverable before the death of the owner/lender can be after death by the deceased's personal representatives - section 131 Income Tax Act 2000 – sections 24 and 253 Taxation of Chargeable Gains Act 1992

UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellants

- and -

PETER L DROWN & MRS R E LEADLEY (as executors of JEFFREY JOHN LEADLEY deceased)

Respondents

TRIBUNAL: MR JUSTICE NEWEY
JUDGE GREG SINFIELD

Sitting in public in London on 23 January 2017
Further written submissions: 20 February 2017

Miss Marika Lemos, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Appellants

The Respondents did not appear and were not represented

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DECISION

Introduction

1. Where an asset has become of negligible value, or a loan irrecoverable, the person who owns the asset or made the loan may be able to claim relief for tax purposes. This case is concerned with the position if the owner/lender has died without making such a claim. Can his personal representatives claim relief?

2. The relevant facts can be stated very shortly.

3. During his lifetime, Mr Jeffrey Leadley invested £25,000 in a company called Datalase Limited ("Datalase") and another £25,000 in a company called Keronite Limited ("Keronite"). He also made a loan of £334,784 to a company called Rollestone Crown Limited ("Rollestone").

4. By 5 April 2010, Mr Leadley's shares in Datalase and Keronite had become valueless and the loan to Rollestone was irrecoverable (Rollestone having gone into liquidation in November 2008 and been dissolved in November 2009).

5. On 6 April 2010, Mr Leadley was served with notice under section 8 of the Taxes Management Act 1970 to file a tax return for the year 09/10. He had not, however, done so by 11 May 2010, when he was killed in a motoring accident. Had he filed a return before his death, he could have claimed relief in respect of both his shares in Datalase and Keronite and his loan to Rollestone.

6. In January 2011, Mr Leadley's executors ("the Executors") filed a tax return reporting his chargeability to tax for 09/10. The Executors originally claimed relief for losses of £384,784, i.e. £25,000 in respect of each of the shareholdings plus £334,784 for the loan. By the time of the hearing before the First-tier Tribunal ("FTT"), however, the issues had narrowed somewhat and it was the Executors' position, first, that £40,000 of the loss on the shares could be set against income arising in 09/10, by virtue of section 131 of the Income Tax Act 2000 ("ITA") and section 24 of the Taxation of Chargeable Gains Act 1992 ("TCGA"), and, secondly, that section 253 TCGA allowed them to carry forward against capital gains in future years the loss on the loan. HM Revenue and Customs ("HMRC") contended that the Executors were not entitled to make either claim.

7. In a decision released on 11 September 2014 ("the Decision"), the FTT (Judge Barbara Mosedale) upheld the Executors' claim for relief in respect of the shares (see paragraphs 59-62 of the Decision). As regards the loan, Judge Mosedale held that the Executors had been entitled to make a loss claim in the return, but that the claim could not be carried forward so as to offset gains incurred by the Executors after Mr Leadley's death (see paragraphs 67-69 of the Decision).

8. With Judge Mosedale's permission, HMRC now appeal against the Decision. The Executors have withdrawn from the proceedings, taking the view that "the tax at stake … is disproportionately small in comparison to the potential costs which could be incurred should the [Upper] Tribunal, and potentially the Court of Appeal, ultimately rule in favour of HMRC". HMRC agreed that, in the circumstances, they would not seek their costs in respect of the proceedings before the Upper Tribunal.

The statutory framework

9. As already indicated, the claim for relief in respect of the shares in Datalase and Keronite depends on section 131 ITA and section 24 TCGA. The former provides, so far as relevant, as follows:

> "(1) An individual is eligible for relief under this Chapter ('share loss relief') if–
>
> (a) the individual incurs an allowable loss for capital gains tax purposes on the disposal of any shares in any tax year ('the year of the loss'), and
>
> (b) the shares are qualifying shares.
>
> This is subject to subsections (3) and (4) ….
>
> …
>
> (3) Subsection (1) applies only if the disposal of the shares is–
>
> …
>
> (c) a disposal within section 24(1) of TCGA 1992 (entire loss, destruction dissipation or extinction of asset), or
>
> (d) a deemed disposal under section 24(2) of that Act (claim that value of the asset has become negligible)."

10. Relief can thus be claimed in relation to "qualifying shares" where, among other things, a loss has been incurred on a "deemed disposal" under section 24 TCGA. That provision, in so far as material, is in the following terms:

> "(1) … the occasion of the entire loss, destruction, dissipation or extinction of an asset shall, for the purposes of this Act, constitute a disposal of the asset whether or not any capital sum by way of compensation or otherwise is received in respect of the destruction, dissipation or extinction of the asset.
>
> (1A) A negligible value claim may be made by the owner of an asset ('P') if condition A or B is met.

(1B) Condition A is that the asset has become of negligible value while owned by P.

(1C) Condition B is that—

(a) the disposal by which P acquired the asset was a no gain/no loss disposal ….

(2) Where a negligible value claim is made:

(a) this Act shall apply as if the claimant had sold, and immediately reacquired, the asset at the time of the claim or (subject to paragraphs (b) and (c) below) at any earlier time specified in the claim, for a consideration of an amount equal to the value specified in the claim.

(b) An earlier time may be specified in the claim if:

(i) the claimant owned the asset at the earlier time; and

(ii) the asset had become of negligible value at the earlier time; and either

(iii) for capital gains tax purposes the earlier time is not more than two years before the beginning of the year of assessment in which the claim is made; or

(iv) for corporation tax purposes the earlier time is on or after the first day of the earliest accounting period ending not more than two years before the time of the claim."

11. Relief in respect of the loan to Rollestone was claimed under section 253 TCGA. The relevant parts of this state:

"(3) Where a person who has made a qualifying loan makes a claim and at that time —

(a) any outstanding amount of the principal of the loan has become irrecoverable, and

(b) the claimant has not assigned his right to recover that amount …

…

> then … this Act shall have effect as if an allowable loss equal to that amount had accrued to the claimant at the time of the claim or (subject to subsection (3A) below) any earlier time specified in the claim.
>
> (3A) For the purposes of subsection (3) above, an earlier time may be specified in the claim if:
>
> (a) the amount to which that subsection applies was also irrecoverable at the earlier time; and either
>
> (b) for capital gains tax purposes the earlier time falls not more than two years before the beginning of the year of assessment in which the claim is made ….”

12. Section 62 TCGA, dealing with death, is also noteworthy. This provides:

> “(1) For the purposes of this Act the assets of which a deceased person was competent to dispose—
>
> (a) shall be deemed to be acquired on his death by the personal representatives or other person on whom they devolve for a consideration equal to their market value at the date of the death, but
>
> (b) shall not be deemed to be disposed of by him on his death (whether or not they were the subject of a testamentary disposition).
>
> (2) Allowable losses sustained by an individual in the year of assessment in which he dies may, so far as they cannot be deducted from chargeable gains accruing in that year, be deducted from chargeable gains accruing to the deceased in the 3 years of assessment preceding the year of assessment in which the death occurs, taking chargeable gains accruing in a later year before those accruing in an earlier year ….”

13. Judge Mosedale noted (in paragraph 49 of the Decision) that “[e]veryone was agreed that the effect and purpose of section 62(1)(a) [TCGA] was to re-value the deceased’s assets at death, wiping out any pre-death gain, in order to avoid what would otherwise be a double charge to tax, as inheritance tax is charged on the estate at death.”

The FTT proceedings

HMRC’s case before the FTT

14. HMRC’s position before Judge Mosedale was essentially that, to make a negligible value claim in respect of an asset, the asset must have been owned

by the claimant when it became of negligible value and still be so owned at the time of the claim. Those requirements were not met, it was argued, in the present case. Although the Executors owned the shares in Datalase and Keronite when the claim was submitted, they belonged to Mr Leadley, and not the Executors, at the point they became of negligible value.

15. In support of these submissions, HMRC pointed out that section 24 TCGA allows a negligible value claim to be made "by the owner of the asset" (section 24(1A)) where the asset in question became of negligible value "while owned by P" (see section 24(1B) TCGA), "P" being the owner of the asset and the person who can make the claim. Here, the owners of the shares and, hence, the persons able to make any claim are the Executors, but the shares were already of negligible value by the time they acquired them. Further, having regard to section 24(2)(b) TCGA, the date specified in a claim cannot be backdated beyond the point at which the claimant acquired ownership of the asset.

16. Similarly, HMRC contended that it was Mr Leadley rather than the Executors who made the loan to Rollestone and to whom it was owed when it became irrecoverable. Only Mr Leadley, therefore, could have claimed relief in respect of it.

The Decision

17. Judge Mosedale did not accept HMRC's contentions.

18. As regards the shares, Judge Mosedale found that "the date of the claim was 5 April 2010 as this was the date set out in the capital gains tax schedule to and filed with the 09/10 tax return" (paragraph 21 of the Decision) and that it would be an "overly literal interpretation of the current legislation to require P to remain the owner of the asset after the date on which the claim is to have effect" (paragraph 25). Accordingly, section 24 TCGA "only required Mr Leadley to be the owner up to 5 April 2010", not at the date the return was submitted (paragraph 27). Moreover, "a purposive interpretation of s 24 TCGA and s 131 ITA is that the personal representatives of the deceased are treated *as* the deceased in so far as they are returning the deceased's own tax liability" (paragraph 59) and, "[a]s the executors do stand in the shoes of the deceased person in so far as his pre-death tax chargeability is concerned, … for the purposes of s 24 the executors are treated as representing Mr Leadley, who was the owner of an asset which became of negligible value while owned by him" (paragraph 60).

19. Judge Mosedale went on (in paragraph 61 of the Decision):

> "However, such a purposive interpretation of s 24 TCGA would not permit the personal representatives to make a claim covering a period after the date of death, because the 'P' at that time would be the personal representatives themselves, as it is their own liability and not the deceased which they would be returning, and the asset would not

have become of negligible value while owned by the personal representatives. Similarly, no s 131 claim could be made by any personal representatives returning their own chargeability to tax in relation to income and gains arising in the estate post the death but utilising losses arising in the deceased's lifetime, as the executors, who would be representing themselves rather than the deceased, have not incurred the loss."

20. Turning to the loan, Judge Mosedale said this:

"66. While the wording of s 253 [TCGA] differs from that of s 24 TCGA and s 131 ITA, the same point arises. Mr Leadley made the loan. At the date of the claim the loan had become irrecoverable. But the 'claimant' is the personal representatives in the sense that it was the executors who completed the 09/10 return, Mr Leadley having died.

67. All the same considerations arise as I have set out above. I consider that a purposive reading of s 253 TCGA should be the same as I have given s 24 TCGA: in other words, the personal representatives are representing Mr Leadley when submitting a return of the deceased's tax chargeability and, as representing Mr Leadley, are able to make, effectively on his behalf, the claims which he could have made had he lived.

68. So it seems to me that the executors could make the s 253 loss claim in the return, and could carry it forward against any future losses incurred by Mr Leadley. I was not informed whether in fact Mr Leadley did incur any losses in the short period after the end of the 09/10 tax year and before his death. However, for the period following his death, Mr Leadley has no tax liability so the tax benefit of the losses to which he was entitled can not be carried forward any further. In particular, they cannot be used to offset any gains incurred by the executors during the period of their executorship.

69. In other words, by virtue of their common law legal status as his personal representatives, the executors stand in the shoes of Mr Leadley and are treated, and were intended by Parliament to be treated, in so far as Mr Leadley's chargeability is concerned, as if they were Mr Leadley. So the s 253 claim could be made in the 09/10 return which returned Mr Leadley's chargeability to tax. But there is no provision to enable a s 253 claim by Mr Leadley (or, as in this case, executors representing him) to be used against the executors' chargeability. So the executors can not use Mr Leadley's (deemed) s 253 claim against their own liability to tax arising out of any gains in the period of their executorship."

The shares

21. Miss Marika Lemos, who appeared for HMRC, submitted that, contrary to Judge Mosedale's view, the date of a negligible value claim must be that of its submission. If, she said, the conditions found in section 24(2)(b) TCGA are satisfied, a claimant can specify an earlier date as that at which the relevant asset is to be deemed to have been sold and reacquired, but that is not the same as treating the claim itself as having been made on a date before that on which it was in fact submitted. The purpose of the legislation, Miss Lemos argued, is to cater for situations in which someone still owns an asset but it has become of negligible value. Where there has been a disposal of the asset, the loss will have crystallised and the "deemed disposal" provisions have no role to play. Miss Lemos also pointed to other situations in which personal representatives are unable to take steps that the deceased could have taken to limit his tax liabilities. Suppose, she said, that someone has a painting which was once worth £100,000 but would now fetch only £10,000. If he sells it just before he dies, there will be an allowable loss which, so far as it cannot be deducted from chargeable gains accruing in that year, can be deducted from previous years' gains (see section 62(2) TCGA), but there will be no such allowable loss if he happens still to have the painting at the time of his death. Conversely, it is easy to envisage circumstances in which the tax payable on a person's estate would be reduced as a result of his failing to dispose of it. We were shown an internal HMRC memorandum dating from 1993 in which the point was put in this way:

> "Thus we have the situation where if the taxpayer is knocked down on her way to her accountant's office to sign a negligible value claim no one can make a capital loss on the asset whereas if she is knocked down after signing the claim a capital loss will be available. This seems extremely harsh.
>
> However the taxpayer could equally have been on her way to sell the asset for £1, realising a large loss, or £1 million realising a large gain. The opportunity to make that gain is lost on death. On her death any losses and gains which may have accrued in assets which she owned disappear as the assets pass at market value to the personal representatives (Section 62 TCGA 1992)."

22. We find Miss Lemos' submissions convincing. We can see no indication in the legislation that a negligible value claim can be taken as made at a time other than that at which it is submitted. While section 24(2) TCGA allows an earlier time to be specified as that of the notional sale and reacquisition, there is nothing comparable as regards the claim itself. Moreover, section 24(2)(b)(iii) and (iv) appear to contemplate a claim being made *during* a year of assessment rather than at its beginning or end. Further, we agree with Miss Lemos that the purpose and wording of section 24 suggest that a claimant must still own an asset at the point a negligible value claim is submitted in respect of it.

23. In arriving at her conclusions, Judge Mosedale referred to the decision of Vinelott J in *Williams v Bullivant* [1983] STC 107. That case concerned section 23(4) of the Finance Act 1965 (a predecessor of section 24 TCGA), which read as follows:

> "If, on a claim by the owner of an asset, the inspector is satisfied that the value of an asset has become negligible, he may allow the claim and thereupon this Part of this Act shall have effect as if the claimant had sold, and immediately re-acquired, the asset for a consideration of an amount equal to the value specified in the claim."

24. Vinelott J concluded, allowing an appeal by the Crown, that there was "no possible ground for construing the subsection in a way which results in that notional sale and reacquisition taking place on a date earlier than the date of the claim by the owner of the relevant asset" (see 111). A little earlier in his judgment, however, Vinelott J had said, albeit obiter:

> "On a literal construction the word 'thereupon' most naturally relates back to the words 'he may allow'. That literal construction may give rise to arbitrary consequences if, for instance, as a result of delay on the part of the inspector, a claim made in one tax year is allowed in a subsequent tax year. In practice, … the Revenue have always construed sub-s (4) as if the word 'thereupon' related back to the words 'on a claim by the owner of an asset'. That, I think, is a permissible construction, and I can see great force in the argument that if it is a permissible construction it should be preferred to a construction which fixed the possibly arbitrary date when the claim is allowed."

25. Having quoted this passage from Vinelott J's judgment, Judge Mosedale said (at paragraph 25 of the Decision):

> "Whereas in that case the judge considered it … overly literal to require the deemed disposal and re-acquisition to be the date the claim was accepted by HMRC, I think here too it is overly literal interpretation of the current legislation to require P to remain the owner of the asset after the date on which the claim is to have effect."

In our view, however, *Williams v Bullivant* does not present any real obstacle to Miss Lemos' case. The interpretation that Vinelott J favoured of "thereupon" was one that he considered to be a "permissible construction". That there are limits to the extent to which the literal meaning of words can be put to one side is apparent from *Williams v Bullivant* itself, where Vinelott J held that the appeal had to be allowed "with some regret" (see 112) because the legislation could not be construed "in a way which results in that notional sale and reacquisition taking place on a date earlier than the date of the claim by the owner of the relevant asset". It is, moreover, noteworthy that, in *Williams v Bullivant*, the date of the relevant claim was evidently taken to be the date of its submission. The inspector had said in a letter that the date for

valuation for a claim under section 23(4) of the Finance Act 1965 was "in strictness the date on which the claim is made, which in this case will be the 27 February 1978".

26. During the hearing, we floated the idea that the solution to the case might lie in identifying Mr Leadley and the Executors. On that basis, it would not matter that Mr Leadley owned the shares when they became of negligible value and the Executors owned them when the negligible value claim was submitted. Treating Mr Leadley and the Executors as one, it could be said both that the claim was made "by the owner" for the purposes of section 24(1A) TCGA (since the claim was made by the Executors) and that the shares had become of negligible value "while owned by P" for the purposes of section 24(1B) (since they were owned at the time by Mr Leadley).

27. In the light, however, of Miss Lemos' further submissions on the point, we have been persuaded that a deceased person and his personal representatives cannot be equated. The TCGA treats the two as distinct and provides, in section 62, for personal representatives to be deemed to acquire the assets of a deceased person on his death for a consideration equal to their market value without a disposal. As Miss Lemos observed, the beginning of the personal representatives' ownership period is demarcated as a matter of law and fact and with specified consequences as regards the application of TCGA. Further, conflating deceased and personal representatives would cause confusion, and potentially anomalies, in other contexts (for example, the availability of investors' relief under chapter 5 of Part V TCGA).

28. In all the circumstances, while we can well understand why Judge Mosedale favoured the construction she adopted, we cannot agree with her interpretation of section 24 TCGA. It seems to us that, here, the possibility of a negligible value claim in respect of the shares in Datalase and Keronite died with Mr Leadley. If that seems an unsatisfactory outcome, there are other situations, as already noted, where the death of an owner of an asset can produce a tax liability lower than would have been the case had the deceased person survived.

The loan

29. Similar arguments arise in relation to the loan to Rollestone. As Judge Mosedale explained (in paragraph 66 of the Decision):

> "While the wording of s 253 differs from that of s 24 TCGA and s 131 ITA, the same point arises. Mr Leadley made the loan. At the date of the claim the loan had become irrecoverable. But the 'claimant' is the personal representatives in the sense that it was the executors who completed the 09/10 return, Mr Leadley having died."

30. HMRC stress that that section 253 TCGA refers to a claim being made by "a person who has made a qualifying loan" and who "has not assigned his right to

recover that amount". In the present case, Miss Lemos said, the claimants (viz. the Executors) had not made the qualifying loan. Furthermore, the person who did make the loan (namely, Mr Leadley) can be said to have assigned the right to recover it to the Executors.

31. Judge Mosedale considered that "a purposive reading of s 253 TCGA should be the same as [she had] given s 24 TCGA" (paragraph 67 of the Decision). As will be apparent, however, we take a different view from Judge Mosedale on the correct interpretation of section 24 TCGA, and we similarly differ from her on how section 253 TCGA should be construed. It seems to us that Miss Lemos' approach to section 253 is correct and, hence, that personal representatives cannot claim relief under the section for loss suffered on a loan made by the deceased person. It follows that HMRC were right to reject the Executors' claim for relief in respect of the shares in Rollestone.

Conclusion

32. We shall allow the appeal. In our view, the Executors were not entitled to claim relief in respect of either the shares in Datalase and Keronite or the loan to Rollestone.

Mr Justice Newey **Judge Greg Sinfield**

RELEASE DATE: 24 March 2017