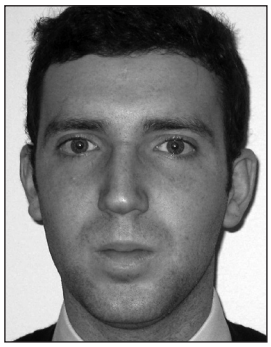
Breaking new ground

Elizabeth Small and Anthony Goodmaker discuss a recent ruling on whether TOGC rules can apply to the grant of a long lease



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'The decision of the *First-tier Tribunal in Robinson Family Ltd v HMRC* is very helpful as there the tribunal held that a grant of a lease could be a TOGC.'

Tax professionals were very excited by the decision in *Robinson Family Ltd v HMRC* [2012] as this marked a fundamental shift in how the majority of us had considered that the transfer of a going concern (TOGC) rules had operated.

Hitherto we had understood that in order to qualify as a TOGC (among other conditions) the buyer had to 'step into the shoes' of the vendor and that involved, in the context of the sale of a property rental business, acquiring the same property interest as the vendor had owned. So if a vendor owned the freehold of a property (subject to and with the benefit of, a lease or leases) he had to sell that freehold interest to the buyer.

Rumours had been circulating that some Inspectors of Taxes had accepted that the grant of a long, ie 999 year lease where the ground rent was minimal could be a TOGC. Sometimes a lessee's advisor would seek to argue this point on the basis that economically the lease in these circumstances was tantamount to a sale and thus should be capable of being treated as though it were a TOGC with the attendant SDLT saving and VAT cashflow benefits. This was never an argument that I accepted however as quite categorically HMRC Notice 700/9/08 stated in para 6.3 (examples where there is not a TOGC):

> If you ... own the freehold of a property and grant a lease, even a 999-year lease, you are not transferring a business as a going concern. You are creating a new asset (the lease) and selling it while retaining your original asset (the freehold). This is true regardless of the length of the lease. Similarly, if you own a headlease and grant a sub-lease, you are not transferring your business as a going concern.

The decision of the First-tier Tribunal in *Robinson Family* is thus very helpful as there the tribunal held that a grant of a lease could be a TOGC.

Turning to the facts of the case, Robinson Family Ltd (RFL) was a development company that had purchased a 125-year interest in a site owned by the Belfast Harbour Commissioners. RFL intended to develop the site into six units and grant sub-leases of these to third parties. The dispute between RFL and HMRC related to one of these units, which RFL had been negotiating to let. RFL would ordinarily have assigned its interest in the 125 lease (subject to the agreement for underlease with the tenant) and subject to satisfying the normal rules regarding TOGCs, this transaction would have been a TOGC. There was however a restriction imposed by the Belfast Harbour Commissioners against any sub-division of the site other than by way of the creation of sub-leases, so rather than sell its interest (in one of the units), RFL had no choice but to grant an interest of 125 years less three days to the lessee, ie quasi-purchaser, subject to and with the benefit of the proposed letting.

HMRC argued that there was no TOGC and pointed to their guidance at para 6.3 referred to above.

RFL appealed to the First-tier Tribunal and argued that the grant of a sub-lease was the only mechanism by which RFL could transfer a part of its letting business to a third party who was a lessee, but for all economic purposes a 'buyer' and that, looking at the substance of the transaction rather than its form, a TOGC had occurred.

The tribunal agreed with RFL and looked at the substance of the transaction to hold that the transferee of the unit was, in effect, carrying on exactly the same business as the transferor so the TOGC provisions should apply.

What has concerned practitioners in the last few months has been as follows:

- that this decision was categorically contradicted by HMRC's views as referred in on para 6.3 above, and, thus, whether HMRC would persist in their views and appeal the RFL decision; and alternatively
- that HMRC would argue that RFL was specific to its facts, ie that the critical point was BHE's prohibition on sub-division and that without that factor RFL's appeal would not have been successful.

It was thus with great relief that I read Revenue and Customs Brief 30/12 and noted that HMRC was not appealing the decision in RFL. But I was also very p leased to note that HMRC's new guidance goes somewhat beyond this decision as HMRC appear to accept that there can be a TOGC in respect of the grant of a lease even where the transferor (ie the effective vendor) is not prohibited from making an outright disposal of his interest.

Instead, HMRC have opined that the relevant factor is whether one can say that economically the

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grant of the lease is tantamount to a sale of the transferee's interest, HMRC are of the view that this is the case where the transferee is left with a less than 1% interest in the property (assessed by value but disregarding any mortgage or charge).

HMRC have gone on to state:

> If the interest retained by the transferor represents more than 1% of the value of the property, HMRC would regard that as strongly indicative that the transaction is too complex to be a TOGC.

HMRC gives the following useful example:

> A owns the freehold of a building valued at £1m which A Ltd rents out commercially. A Ltd sells that property rental business by granting to B Ltd a 999-year lease under which A Ltd is entitled to receive a ground rent of £100 each year. The value of that right, together with any and all other rights retained by A Ltd, is £2,000. Provided all the normal conditions are satisfied, the transaction will be a TOGC, because HMRC will regard the 0.2% interest retained as too small to disturb the substance of the transaction.

Where more than one property is being transferred, the test is to be considered taking each property in turn, not with regard to an overall transfer of several properties.

HMRC have stated that none of their other opinions regarding TOGCs have been changed by this ruling but that they are considering whether:

- on the surrender of a lease there could be a TOGC; and
- whether the decision in RFL has application to transfers of businesses that are not property rental businesses.

It will be interesting to see how HMRC's thinking develops in these and other areas and I anticipate, in the light of this decision, that a surrender of a lease which is subject to, and with the benefit of, occupational leases should be a TOGC. Meanwhile I expect that a lot of practitioners will be reviewing their old files to see if any claims for repayment of VAT and possibly SDLT thereon can be made.

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There may be many situations where, under the new guidance, there could have been a TOGC but instead, because the property had been opted for VAT purposes, there was a standard rated supply with VAT paid by the transferee and the transferee has also paid SDLT on the VAT inclusive amount. But files have to be checked carefully before making claims to HMRC. In particular, were the other conditions for being a TOGC present? It is also worth highlighting the need to act expediently in pursuing claims against completed transactions, bearing in mind the relevant time limits that will apply.

Readers will be aware that one of the other conditions for there to be a TOGC is that the transferee must give notification to the vendor on or before the tax point (usually the date of completion) that an option to tax will not be rendered ineffective (see Articles 5(2A) and 5(2B) of the VAT (Special Provisions) Order 1995 as set out in para 11.2 of HMRC Notice 742A (option to tax land and buildings).

In the recent press release, HMRC have said that provided the parties can satisfactorily evidence that Article 5(2B) did not apply at the time of the transaction and that therefore the requisite notification could have been given, HMRC will accept that this requirement for TOGC status has been complied with.

But note that this is the only TOGC condition that HMRC has stated that they will deem to be satisfied and so if, for example, a transferee had not been a taxable person or had not opted to tax the building (where the transferor had opted) at the relevant date, ie usually completion, then it would not be possible to make the grant of that particular lease a TOGC.

HMRC have stated that they are considering the question of whether an adjustment can be made to the SDLT already paid and that they will shortly be issuing some further guidance on this matter. I consider it is surprising that this guidance was not contained in this release from HMRC.

While I applaud the decision and HMRC's response to it, I am nervous in celebrating the general current trend of the Tribunal and HMRC moving ever more towards a substance/purposive approach to law. Here it has worked in the taxpayers' favour, but this will not always be the case and this, together with the constantly shifting sands of tax law means that this is less and less certainty that we can offer our clients. ■

Robinson Family Ltd v HMRC [2012] UKFTT 360 (TC), TC02046