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Indirect Tax



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Georgina West considers the impact of the *Project Blue* decision on how SDLT now applies to complex transactions

Key Points

What is the issue?

Two issues arose from this case: whether both sub-sale relief and the exemption for alternative property finance applied, and, if so, how the SDLT anti-avoidance

provision in FA 2003 s 75A should apply to the transaction.

What does it mean to me?

It is going to be difficult to sustain the argument that deliberate avoidance of SDLT is all that can be caught by s 75A.

What can I take away?

Advisers will need to consider carefully how the rules apply and, how and if they can manage their clients' risk, bearing in mind that HMRC Stamp Taxes policy to date has been to refuse to provide clearances on the application of s 75A.

Thankfully from a complexity perspective, FA 2003 s 75A (s 75A) only applies to SDLT and there are no equivalent provisions under Welsh land transaction tax or Scottish land and buildings transaction tax. As such section s 75A can only now apply to real estate situated in England and Northern Ireland or to certain partnerships owning such real estate.

The provisions of s 75A have only been considered in a small number of cases. The most notable example (and the most detailed) is the Supreme Court judgment in *Project Blue Limited v Commissioners for Her Majesty's Revenue and Customs*. The outcome of the case raises a number of concerns for taxpayers. On 5 April 2007, Project Blue Limited ('PBL') and the Ministry of Defence ('MoD') entered into a contract for PBL to purchase the former Chelsea barracks for £959m. Subsequently, PBL contracted to sell the freehold to MAR and MAR agreed to lease the barracks back to PBL. Upon completion, the following occurred:

MAR and PBL entered into put and call options requiring/entitling PBL to repurchase the freehold in the barracks;

a) the MoD conveyed the barracks to PBL;
b) PBL conveyed the barracks to MAR; and
c) MAR leased the barracks back to PBL.

Actions (a), (c) and (d) were taken to facilitate ijara financing (a form of Islamic financing).

PBL and MAR submitted that no SDLT was due, on the basis of sub-sale relief applying (in the case of PBL) and Alternative Property Finance Relief applying (in the case of MAR and the PBL lease). In the absence of s 75A the Supreme Court held that the planning would have been successful. Most notably the Court found that when considering the application of clauses it is important to consider whether real-world or SDLT terms are used. In particular, Alternative Property Finance Relief (s 71A) was available since the vendor and purchaser under that relief are identified using the real-world situation irrespective of the fact that the deeming provisions in section 45 (which use SDLT terms) deemed the vendor to be somebody else. However, the taxpayer lost the case due to the application of s 75A. Broadly, s 75A applies where:

- one person (V) disposes of a chargeable interest and another person (P) acquires it (or an interest derived from it),
- a number of connected transactions are *involved in connection with* the disposal and acquisition (the 'scheme transactions'), and
- the sum of the amounts of SDLT which is payable as a result of the scheme transactions is less than would have been payable on a notional transaction.

Where there is more than one land transaction, the court held that the task, when identifying who V and P are, is to identify where the tax loss has occurred as a result of the scheme transactions. Where P is concerned this is by 'identifying the person on whom the tax charge would have fallen if there had not been the scheme transactions which … exploited a loophole'. Where benign transactions are occurring, and there is no exploitation, it would seem that a common-sense approach should be taken. Although it was held that adopting a sequential approach to determining who V and P are was not appropriate for the facts in Project Blue, it may be appropriate to consider who starts with the property (as V) and who ends up with the substantive interest in the property (as P) or to take a different view in context of the facts.

The term 'scheme transaction' is very widely drafted (and includes things that would not otherwise be regarded as transactions). As the term 'in connection with' is not defined it must be given its everyday meaning, and this approach has been supported by a number of cases. Although the term 'in connection with' has been held in other cases to extend to matters outside (but connected to) the whole (and not just parts of the scheme) and it has been accepted that Parliament did not intend connection to be limited to direct connections, the use of the word 'involved'

reduces the potential ambit of s 75A as it denotes some form of participation. The First-tier Tribunal (in Project Blue) held that: 'The linkage must be more than merely being a party in a chain of transactions and the test must be more than a "but for" test (or, as the classicists would put it, a sine qua non test) otherwise the word "involved" would be deprived of significant meaning.'

However, in *Geering & Ors v HMRC* the FTT held that it was not necessary for the vendor to have knowledge of the other transactions for the provisions of s 75A to be engaged. However, in the author's view, transactions which the vendor may have carried out in connection with the disposal, but that the purchaser is not aware of (and should not have been reasonably aware of), should not generally be scheme transactions.

When looking at the application of s 75A the courts held in Project Blue that, because 'there is nothing in the body of the section which expressly or inferentially refers to motivation' the test as to whether s 75A was engaged was whether the SDLT payable under the actual scheme transactions was less than that payable under the notional transaction. In other words, s 75A applies in a purely mechanical way and can apply even in the most benign of circumstances where a land transaction involves more than a single step or transaction.

Where s 75A applies a notional transaction is postulated. The consideration for the notional transaction is the largest amount (*or aggregate* amount):

(a) given by or on behalf of any one person by way of consideration for the scheme transactions, or
(b) received by or on behalf of V (or a person connected with V) by way of consideration for the scheme transactions.

However, amounts given as consideration under certain scheme transactions can be discounted where they are incidental transactions. Although the legislation provides very limited examples of what is incidental, and these may not be of much practical use in most cases, they are merely examples. Project Blue held that a purposive view of the legislation must be taken. This may enable a wider range of amounts to be taken out of consideration.

Furthermore, where there are a number of assets being transferred it should be possible to allocate any consideration (arising under the notional transaction) between the assets on a just and reasonable basis. There is nothing within s 75A to

prevent the just and reasonable apportionment provisions (in paragraph 4 schedule 4) applying to the notional transaction. On a purposive reading, this would prevent SDLT arising on benign transactions which involve, say, a transfer of business assets which happen to include real estate. Against this, taxpayers may want to consider whether the inclusion of section 75C(5) erodes that argument.

Where the consideration payable for the notional transaction exceeds that payable under the actual transaction SDLT will be payable on the notional transaction irrespective of whether that amount exceeds the value of the property or the consideration given on an arms-length basis. This was, in fact, what happened under Project Blue and, had it not been for the fact that amounts were not drawn down and for exchange rate movements, c£50m of SDLT would have been payable (which would have exceeded the SDLT which MAR would have paid in the absence of undertaking the scheme by c£12m).

The aggregation clause also heightens the risk of SDLT being calculated on more than the market value of the property or the amounts commercially agreed between the parties (even under benign transactions).

Where there are more complex arrangements under which no other assets pass there may be no basis for a just and reasonable apportionment. This may be particularly relevant to public sector transactions (which by their very nature are complex and within the ambit of s 75A). The author considers that some comfort may, however, be drawn from the incidental transaction carve out provisions.

Whilst the notional transaction can benefit from any relief that the actual transaction affords, it is necessary to consider the availability of these reliefs as at the date of the last scheme transaction. Furthermore, the identification of V and P may also taint the availability of reliefs. It is also worth remembering that the partnership rules (in paragraph 15 schedule 15 FA 2003) no longer apply to the notional transaction (although a transfer of property investment partnership is still within the ambit of s 75A).

Where s 75A applies, a land transaction return may be required for the notional transaction. This is particularly the case where V and P are different parties to those who would otherwise be making SDLT returns.

Taxpayers will need to consider carefully how the rules apply and how and if they can manage their risk, bearing in mind that HMRC Stamp Taxes policy to date has

been to refuse to provide clearances on the application of s 75A (and HMRC's guidance is currently out of date). Warranty & Indemnity insurance may be impossible to obtain to cover some s 75A risks, as insurers will not cover a risk if it cannot be adequately quantified or is potentially too high.

Taxpayers also need to consider whether additional disclosure (by way of a 'Veltema' letter) is required, or desired. This may particularly be the case where taxpayers wish to limit their enquiry window and/or there are complex facts or arguments.

In some cases, taxpayers may simply be forced to abandon deals either because of uncertainty or because s 75A simply imposes a charge to SDLT above and beyond the value of the property.