Unjust you waited, Mr Higgins

Management of taxes | Personal tax



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Keith Gordon looks at a case which considers the ‘period of ownership’ for the purposes of main residence relief

Key Points

What is the issue?

Mr Higgins purchased a (not yet built) flat. HMRC contended that the exemption available to Mr Higgins should be restricted because the period of occupation (two years) was considerably less than the period between the deemed acquisition in late 2006 and the disposal. However, Mr Higgins was unable to live in the flat during the whole period of ownership because the flat was not yet built.

What does it mean to me?

The First-tier agreed with Mr Higgins but HMRC appealed against that decision to the Upper Tribunal. The Upper Tribunal reversed the decision.

What can I take away?

It is essential that advisers ensure that all facts relating to acquisitions and disposals of properties are established.

One of the few constants in the world of UK tax is the notion that an individual's home should not be subject to capital gains tax when it is disposed of. Of course, the rule is in practice more complicated than that but the exemption of one's main home is clearly the underlying principle. (Out of interest, the statutory phrase used for the relief refers to an individual's 'Only or main residence' – the widely-used phrase 'principal private residence' has no real statutory basis.) At its simplest, the relief ensures that any gain arising during the period of ownership remains outside the tax net.

So as to reduce the impact of what has in recent years become known as 'flipping', the exemption is limited in most cases where the property did not constitute the individual's only or main home throughout that period of ownership. Subject to certain statutory modifications (particularly the final part of period), the exemption applies only to the proportion of the period of ownership for which the 'only or main residence' test is met.

It might be thought that there could be little doubt as to the meaning of 'period of ownership'. However, tax is rarely that straightforward. In particular, Taxation of Chargeable Gains Act 1992 section 28 provides that an acquisition (or disposal) is deemed to take place at the earliest time when the relevant transaction becomes unconditional. The recent case of *HMRC v Higgins* [2018] UKUT 280 (TCC) concerns the interaction of these two provisions.

Facts of the case

In 2004, Mr Higgins paid a deposit of £5,000 to secure an apartment which was as then unbuilt.

Two years later he entered into a formal agreement for the purchase of the apartment which, then, was still unbuilt – generally referred to as ‘exchange’. At the time, he paid a further £52,500 (representing 10% of the £575,000 purchase price less the deposit already paid). He paid a further 10% in March 2007, with the remaining 80% (£460,000) payable on completion.

Work did not start on the construction until a later date and the apartment was substantially completed by December 2009, with legal completion to follow in January 2010 when Mr Higgins duly moved into the property and occupied it as his only or main residence.

In December 2011, Mr Higgins exchanged contracts for the sale of the apartment and this sale was completed in January 2012 at which time Mr Higgins ceased to occupy it.
HMRC contended that the exemption available to Mr Higgins should be restricted because the period of occupation (two years) was considerably less than the period between the deemed acquisition in late 2006 and the disposal. In contrast, Mr Higgins contended that the period of ownership (the phrase used in the exemption) should take its ordinary meaning and run only from the date of completion of the purchase. The First-tier agreed with Mr Higgins but HMRC appealed against that decision to the Upper Tribunal.

The Tribunal’s decision

The case came before the then President of the Tax and Chancery Chamber of the Upper Tribunal (Mrs Justice Rose) sitting with Judge Jonathan Cannan.

Having considered a number of the main capital gains tax cases over the years (*Jerome v Kelly* [2004] STC 887, *Underwood v HMRC* [2009] STC 239, *Chaney v Watkis* [1986] STC 89), the Upper Tribunal allowed HMRC’s appeal.

The essence of the Tribunal’s reasoning appears to be that the chargeable gain (before any exemption) is computed (broadly) by reference to the amounts contractually agreed on the acquisition and disposal and that s 28 similarly fixes the

dates of acquisition and disposal to be those dates on which the respective agreements become unconditional. Furthermore, given that the statute is clearly providing that there should be a reduction of relief in cases where a property is not occupied as a main residence throughout the period of ownership, there is nothing unfair about the outcome in the present case.

Commentary

I must admit that when reading the First-tier's decision, I considered it to representing a common sense response to what is perhaps an increasingly common situation and ensuring that it does not become an increasingly common problem. Essentially, it recognises that it is somewhat difficult for an individual to move into a property (and to occupy it as a residence) before it is even built. Indeed, it recognises that it is practically difficult to move into any property before legal completion of the acquisition.

More importantly, the statutory phrase 'period of ownership' is not actually defined within section 28 – that section merely deems when an acquisition or disposal takes place. Accordingly, the First-tier did not feel constrained to define period of ownership by reference to the deemed dates in section 28.

Now that the Upper Tribunal has reversed the decision, do I now realise that I was wrong? By George, no. I have still not got it. The more I read the Upper Tribunal's decision, the more convinced I am that it was wrong and that the matter should (if there is enough at stake to make it worth it) progress to the Court of Appeal.

As was put beyond doubt by the House of Lords in J*erome v Kelly*, the effect of section 28 is merely to fix the time of an *actual* disposal or acquisition; it does not in itself *effect* any such disposal or acquisition. It seems odd that this limited (although clearly fundamental) provision should have the effect of starting (and ending) the period of ownership for the purposes of the main residence relief when, in virtually all cases, actual occupation will run from (and to) different dates. This is particularly the case given that the restriction on the main residence exemption operates, in practice at least, by reference to *occupation*. The argument in my view is even more compelling given that section 28 was introduced into the statute some six years after the exemption was first enacted and, yet more so, given that the phrase 'period of ownership' has always had its own specific definitions.

What to do next

Given the fact that tax law (generally, and even more so in the light of this case) operates in a world far divorced from reality, it is essential that advisers ensure that all facts relating to disposals of properties are established. If an adviser asked Mr Higgins for the period of ownership he would naturally have pointed to the two-year period between completion of the purchase and completion of the disposal. Indeed, those were the only two years in which he was entitled to occupy the property. As much as we might wish to use ordinary terms (such as period of ownership) when communicating with clients, such user-friendliness can give rise to the wrong information being provided to us. I have no problem with using such terms but that cannot be at the expense of seeking the actual information required under the law.

In the meantime, we should all hope that the Court of Appeal will review this decision and, if not, seek a change in the law.