TAXAdviser

Buzzoni opportunities

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Emma Chamberlain examines the wider implications of the decision in the Buzzoni case

What is the issue?

HMRC argue that there is a reservation of benefit in relation to all home loan schemes; for loans that are repayable on demand, they argue that the failure of the donee to call in the loan confers a direct benefit on the donor

What does it mean for me?

There are two situations where reversionary leases (both pre- and post-1999) are not caught by the anti-Ingram legislation in FA 1996 s 102A

What can I take away?

There are four ways in which reversionary leases can still be used in IHT planning, despite the introduction of pre-owned assets income tax

In the December issue of *Tax Adviser* I reviewed the *Buzzoni* case, which concluded that there is no reservation of benefit (ROB) if a benefit received by the donor did not affect the donee's enjoyment of the gifted property.

The approach of HMRC post-Buzzoni

The unique feature of the case was:

'The covenants contained within the underlease made no difference to the donee's enjoyment of the property transferred because the underlessees, under the licence to underlet, had already entered into covenants direct with the head lessor. The underlessees were already burdened with the obligations given to the head landlord.'

In the case of a freehold interest out of which a reversionary lease has been carved, the only obligation imposed will be under the terms of the lease. It is therefore important that leases do not include an obligation to keep the property in repair. Nor should the leaseholder (the donee) improve the property.

However, the decision in ***Buzzoni v HMRC* [2013] EWCA Civ 1684** [1] – that there must be some detriment to the donee – may have wider implications. Take the example of home loan schemes (sale of a home in consideration of an IOU that is then given away: HMRC argue that there is a ROB in the loan that is repayable on demand because the failure of the donee to call in the loan confers a benefit on the donor who can then continue to occupy the home. However, in many cases the loan note was structured to secure a much lower return if it was called in before the donor died. On that basis there is no detriment to the donee by failing to call in the loan even if there is a benefit for the donor in it remaining outstanding.

In fact, by failing to call in the loan while the donor is alive there is a positive benefit for the donee. Whether this argument will be pursued in the event of litigation on such home loan schemes remains to be seen. So far no cases have gone that far.

The future for reversionary leases

Buzzoni was an arrangement before the anti-*Ingram* legislation in FA 1999 (see FA 1986 s 102A–C). HMRC originally considered that the legislation to stop Ingram arrangements also caught reversionary lease schemes. On that basis reversionary lease schemes effected from 9 March 1999 were caught by reservation of benefit and therefore were not subject to POAT (see **IHTM14360** [2] which has not been updated). This view was not shared by most practitioners and, in a change of heart, HMRC announced on 27 January 2007:

'For reversionary lease schemes entered into on or after 9 March 1999 HMRC had previously held the view that section 102A Finance Act 1986 would apply because the donor's occupation would be a "significant right in relation to the land". If that analysis were correct, the reservation of benefit rules would apply and there would be no income tax charge. However, HMRC now consider that where the freehold interest was acquired more than seven years before the gift, the continued occupation by the donor would not be a significant right and, contrary to its previously held view, section 102A cannot apply to the gift because of section 102A(5). If the donor grants a reversionary lease within seven years of acquiring the freehold interest, section 102A may apply to the gift depending on how the remaining provisions of that section apply in relation to the circumstances of the case.'

Subsequently, the *IHT Manual* was revised (see **IHTM44102** [3] in the section dealing with the pre-owned assets income tax charge) and the following sentence was included:

‘It follows that if the donor grants a reversionary lease within 7 years of acquiring the freehold interest, FA86/S102A may apply to the gift depending on how the remaining provisions of that section apply in relation to the circumstances of the case – for example, if the donor pays full consideration for the right to occupy or enjoy the land, that would not be a significant right in view of FA86/S102A(3), so the reservation of benefit rules cannot apply and a POA charge arises instead.’

There are therefore two situations where reversionary leases are not caught by the anti-*Ingram* legislation in FA 1996 s 102A.

First by s 102A(5), ‘a right or interest is not significant if it was granted or acquired before the period of seven years ending with the date of the gift’. In many cases, persons wishing to enter into reversionary lease arrangements will do so in relation to property that they have owned for at least seven years. In such cases the s 102A(5) let-out applies and the gifted lease is not property subject to a reservation.

Second, s 102A(3) excludes a right interest or arrangement, which enables the donor to occupy the land ‘for full consideration in money or money’s worth’. If Mr X had originally purchased his freehold interest (whether or not within seven years of the date of the gift) for full consideration then this let-out applies so that again the arrangement is outside the amended reservation of benefit legislation.

Reversionary lease schemes have a place in future tax planning in four cases:

1. If there is a pre-March 2006 interest in possession trust in which the life tenant is not the settlor, is elderly and occupies a trust property. He will not have purchased the freehold but he will generally have had a right or interest in the freehold for more than seven years.

2. In relation to IPDI trusts set up in a will, often in favour of a surviving spouse. Although neither the s 102A(3) nor (5) let-outs applies here, FA 1986 s 102ZA (that deems the life tenant to make a gift of the underlying settled property when his IIP is terminated) is not subject to the anti-*Ingram* legislation and therefore the ROB position must be judged solely on the basis of whether s 102 is satisfied. S 102A is only in point in relation to actual gifts of land made by individuals, not to deemed gifts of land made by life tenants.

In both cases a long lease could be granted to the children with the life tenant retaining an IIP in the freehold. As in the previous case, he should not be subject to POAT because he is not making a disposal of an interest in land (or at least nothing of value).

3. In respect of let land when the POAT provisions do not apply.

4. For non-residents because the POAT charge does not apply.

Final observations

As noted in my December article, the ROB rules can be penal in effect, denying spouse exemption or any capital gains tax uplift. What happens if the circumstances of the donor change and he can no longer afford to live in his own property and wishes to move back into the house he gave away many years earlier?

Sch 20 para 6 contains two important statutory let-outs to prevent a reservation of benefit in such circumstances. The first is well known and is called the full consideration exemption. It requires the donor to pay a full market rent for his occupation.

HMRC note at IHTM14341:

‘As a general rule, it is unlikely that any such arrangement could be overturned if the taxpayer can demonstrate that it

resulted from:

- a bargain negotiated at arm's length by parties who were independently advised and
- which followed the normal commercial criteria in force at the time it was negotiated.'

Thus, if the donor pays a full market rent for his occupation, there is no reservation of benefit. The rent must be reviewed each time the agreement is renewed.

The second let-out is less well known and is found in Sch 20 para 6(1)(b): namely, occupation of land by the donor is disregarded if these conditions are satisfied:

'(i) it results from a change in the circumstances of the donor since the time of the gift, being a change which was unforeseen at that time and was not brought about by the donor to receive the benefit of this provision; and
(ii) it occurs at a time when the donor has become unable to maintain himself through old age, infirmity or otherwise; and
(iii)it represents a reasonable provision by the donee for the care and maintenance of the donor; and
(iv)the donee is a relative of the donor or his spouse [or civil partner].'

Note that this exemption does not apply if the donee does not take full possession and enjoyment. In short, it can protect the donor from a reservation of benefit under s 102(1)(b), but not under s 102(1)(a).

This exemption might be more apposite in modern families than is sometimes realised. Consider the scenario in which a donor effected an *Ingram* arrangement 20 years ago, thinking that he would move out at the end of 20 years and live in a small flat elsewhere. Just before the expiry of the lease the donor has a fall, which results in his sudden incapacity. The family do not want to put him in a care home and therefore they decide to allow him to continue living independently with in-house nursing care funded by the donor.

This would appear to fall within the scope of the above exemption.

FURTHER INFORMATION

Read Emma's co-authored book, *Trust Taxation and Estate Planning*, 4th edition (Sweet & Maxwell), ISBN: 9780414028548.

Links
[1] https://www.lexisnexis.com/tolley/library/results/docView/Z-WW-W-W-W-MsSAYWC-UUV-U-U-WCU-U-U-W-AVWACYWBZC-AVAEAZBAZC-VBCAZCCYU-WCU-U?_digest=783d4043c7f022405f55428f3281616488feb5c&csi=279841&docNo=1
[2] http://www.hmrc.gov.uk/manuals/ihtmanual/ihtm14360.htm
[3] http://www.hmrc.gov.uk/manuals/ihtmanual/ihtm44102.htm