

CTT clawback

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An income tax investigation by HMRC has uncovered an undeclared capital transfer tax liability on a lifetime gift made in 1979. Can HMRC still assess this liability or is it out of time because more than 20 years have elapsed?

We recently finalised a tax investigation in relation to a failure to disclose interest on an offshore bank account.

The source of the capital in the account (approximately £100,000) was a gift made to our client by his father back in 1979. The father died in May 1987, his wife having pre-deceased him many years earlier.

The father was a working farmer at the time of his death and, apart from the £100,000 gift, the only other assets of significance would have been the farmhouse and farm lands (estimated value £150,000). There were, as we understand it, no other lifetime gifts.

While we did not act for the father, it is our understanding that no return was made to the Revenue in relation to the lifetime gift and furthermore that an estate return was submitted at death showing nil tax payable.

HMRC Inheritance Tax have now made contact – presumably following up a submission from their income tax colleague.

Basically, they contend that the 1979 transfer by the father was chargeable when made and is subject to capital transfer tax at the lifetime rate.

Our working assumption has always been that a 20-year time limit operates across all taxes.

Do HMRC still have taxing rights in this instance? If not, what support – statutory or otherwise – is available to refute the inspector's assertions?

Query 17,400 – Grand Slam Green

Reply by Hold Fast

I think HMRC are right. Time limits apply for capital transfer tax and inheritance tax where an account was delivered. But no account was delivered following the lifetime gift and so HMRC knew nothing about it until the offshore disclosure was made.

Therefore, one can see why time limits run from the date HMRC became aware of the problem.

The recently published *Compliance Checks: The Next Stage: Draft Legislation and Commentary* (Feb 2009) outlines proposals for changes to time limits for, among other taxes, inheritance tax.

The commentary on IHTA 1984, s 240 says that 'it should be noted that it is not presently proposed to introduce a time limit into s 240(1).

It follows that in a case where no account has been delivered, no time limit will apply to the recovery of underpaid inheritance tax'. IHTA 1984, s 240 is identical to s 240 in the consolidating Capital Transfer Tax Act 1984, which came in turn from FA 1975, Sch 4 para 23(1). HMRC are applying the legislation in this case.

The time limits Grand Slam Green has in mind apply to taxes other than capital transfer tax and inheritance tax – although even there HMRC has rather longer to assess.

If a loss of tax is attributable to fraudulent or negligent conduct by the taxpayer or someone acting on his behalf, HMRC can go back 20 years, 10 months for income tax, PAYE and capital gains tax and 21 years for corporation tax.

The time limits for VAT were 20 years if the conduct was dishonest, the trader was convicted of fraud or a penalty arose under VATA 1994, s 67, and three years if there was a mistake or failure.

New time limits were introduced by FA 2008, Sch 39 from 1 April 2009 for VAT (while ensuring that no earlier period can be assessed than could have been under the old rules) and from 1 April 2010 for income tax, capital gains tax and corporation tax (while leaving it possible to assess and repay non-self assessment PAYE taxpayers for six open years until 31 March 2012).

The new time limits that apply from the end of the accounting period or tax year are four years – normal discovery time limit; six years – careless error (except for VAT, which is four years); and 20 years – deliberate error, failure to register for VAT, failure to notify chargeability to tax, failure to notify tax avoidance schemes.

The Limitation Act 1980 applies to the recovery of debts in England and Wales. Section 37(2) says that tax and other duties and interest on these amounts which are due to the Crown are specifically excluded from its provisions.

So Grand Slam Green could not argue that the capital transfer tax was covered by the Limitation Act – unless this is a Scottish case. Then the Prescription and Limitation (Scotland) Act 1973, s 7 allows 20 years to collect debts.

There is no specific Crown exemption in Scotland, so one could argue that the 20-year period has long elapsed– but even then one would need to show the capital transfer tax obligation became enforceable back in 1979.

That leaves a discussion with HMRC on whether it is reasonable to pursue this capital transfer tax, and presumably interest, after all this time. The *Inheritance Tax Manual* at IHTM30508 outlines circumstances where remission of tax might be considered.

The categories that might be relevant are hardship, miscellaneous and other (the latter is used for the remission of interest). As the interest on these funds was not declared at the right time HMRC are unlikely to be sympathetic but it is still worth a try.