

## **Pre-owned assets following the Finance Bill 2007**

The Finance Act 2004 introduced the legislation relating to pre-owned assets which was broadly designed to collect some tax on an annual basis from those who had successfully avoided the gift with reservation provisions for inheritance tax. The Government thought that they had offered a reasonable 'get out' provision in the form of an election which could be made to treat the arrangements as being caught by the gift with reservation provisions, even though on the facts they were not. This puts the matter back within the inheritance tax regime, and out of the scope of the pre owned asset charge. Unfortunately, the election method out of the problem does not unscramble any capital gains tax downsides in the particular scheme involved, and so the election was not usually the best thing to do. Instead, it was preferable to unwind the scheme.

There are, however, many arrangements which are in grey areas of the pre-owned asset rules and one cannot necessarily be certain whether one is caught or not. Suppose that I gave a large sum of money to my son five years ago and he now buys a house in which I can live. The Inland Revenue will say that this contravenes the contribution condition in the pre-owned asset rules and the idea is caught. This may well be the case if one can clearly show that the money I gave my son is the money which was used to purchase the property, but supposing he is wealthy in any event and did not use the money I gave to finance the property, but used other resources. Is the contribution condition satisfied then? One might take the bold view that it is not and not make any declaration to the Inland Revenue.

Taxpayers may have felt encouraged to take their own views about the scope of the pre-owned asset charge by clause 65 of the Finance Bill 2007. This relaxes the time limit for electing into the gift with reservation rules and out of pre-owned asset tax. Previously the election had to be made on or before the relevant filing date for the tax return unless one could show reasonable excuse. The reasonable excuse provision has now gone and been replaced with a general rule that the election can be made at such later date as an officer of Revenue & Customs may in a particular case allow. So in relation to the idea mentioned above of my son now buying me a house in which I will live, I might think that I can now wait and see if there is an appeal case in the future which will give me better guidance about whether or not this plan is in fact caught by the pre-owned asset rules. If it is, I would hope to be able to make a late election which will retrospectively rub out all past income tax liabilities.

Unfortunately, it seems that clause 65 of the Finance Bill is intended to make very little difference at all. The Inland Revenue has put out some guidance concerning the circumstances in which a late election will be accepted in the future and this includes all the standard statements about postal disruptions, papers being lost through fire or flood and the chargeable person being so seriously ill that he was prevented from dealing with the election at the proper time. The final paragraphs of the guidance contain the following ominous statement: 'We will only accept a late election where the chargeable person

can show that their failure to elect by the relevant filing date is not a result of: (a) their taking active steps to avoid both an income tax charge under this schedule and an inheritance tax charge by virtue of the gift with reservation provisions; (b) the wish to avoid committing to either an income tax charge or an election pending clarification of the effects of making such a commitment.'

In view of these remarks, it is hard to see how the Finance Bill is making any real change to the pre-owned asset election provision. This is just reasonable excuse by some alternative wording. It seems therefore that the Finance Bill clause will still not solve the problems of those who do not know whether they are caught by the pre-owned asset rules or not. As another example, some agents are advising that an old property which still has asbestos in certain parts of it is unlettable and so the rental value for the purposes of the pre-owned asset rules must be within the de minimis limit; but other agents are advising that such a property is lettable and at full market value. If one follows the advice of the agent who says that the property is unlettable, I am not sure that the Finance Bill clause will allow one to elect back into inheritance tax in the future if that advice turns out to be incorrect.

### **Parmentier Arthur Group Plc**

**90 Long Acre  
Covent Garden  
London  
WC2E 9RZ**

**7 The Waits  
St Ives  
Cams  
PE27 5BY**

**Tel: 020 7849 3018**

**Tel: 01480 465522**

**Fax: 020 7849 3171**

**Fax: 01480 461221**

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