SUMMARY ADVICE

Cotswold Barristers Limited (“CBL”) and Property 118 Limited (“P118L”)

Comments from Tax Policy Associates Ltd.

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A general comment: this opinion is addressing limited instructions that relate to a theoretical set of arrangements and not any of the individual clients. It does not consider whether Property 118 structure breaches the terms of their clients' mortgages and leads to a mortgage default. It does not consider whether any anti-avoidance provisions are engaged, or whether the arrangements are within scope of DOTAS. It does not provide a view on the SDLT or IHT points. These omissions are surprising given that these are the most serious problems with the scheme.

Introduction

1. We are instructed to advise (in summary) on whether or not a method of incorporating an unincorporated business (presented under the name “Substantial Incorporation Structure”) is effective for tax purposes in the manner intended by CBL and P118L (together “the Advisors”).

We don't have the instructions put to the KC – we don't know the questions she was asked, or what she was asked to assume. We would speculate that she was asked to assume the structure did not involve tax avoidance (we cannot believe she forgot to mention avoidance issues). This is the elephant in the room – see further below.

We also don't know what the “manner intended” is. This seems important.

2. The request for our advice arises in the context of comments on the structure which have been made by Dan Neidle (“DN”) from Tax Policy Associates (“TPA”).

Dan Neidle takes sole responsibility for all the work of Tax Policy Associates, but it reflects the consensus view of a team of highly experienced tax advisers.

Sixteen tax advisers contributed to our work on Property118, including KCs, solicitors, tax accountants and retired HMRC officials. We can't name most of them for professional reasons, but the two we were able to name, Sean Randall and Pete Miller, are well-

known and respected advisers. Sean is Chair of the Stamp Taxes Practitioners Group, a Fellow of the Chartered Institute of Taxation and author of the leading textbook on stamp duty. Pete is editor/author of numerous leading tax textbooks that are directly relevant to the points at issue. This response also benefits from review by Ray McCann. Ray is a past President of the Chartered Institute of Taxation and worked for many years as a senior HMRC inspector. During his time at HMRC he oversaw the introduction of DOTAS.

Anyone viewing the threads on LinkedIn and Twitter will see a (rare) consensus amongst tax professionals: this structure does not work. A regular comment is that professionals have been waiting for Property118 to be "found out".

3. Our advice is provided to the Advisors only; our advice is specifically not provided to end users of the Advisors' advice or services nor for implementation purposes. No person other than the Advisors may rely upon our advice. No person other than the Advisors may share or publish our advice or make it in any way available in the public domain.

This report provides no legal comfort to Property118's clients. It may put them in a worse position, by giving Property118 an additional defence in the event their clients end up suing them for negligence – "we were following a KC's advice".

Nor can Property118's client believe what they are told about insurance:

> ***If you engage Cotswold Barristers, your Barrister will advise on, adopt and execute my recommendations as their insured legal advice.***
>
> Cotswold Barristers are regulated by the Bar Standards Board and each of their fully qualified and suitably experienced Barristers carries £10,000,000 of Professional Indemnity Insurance per client, meaning that you are shielded from financial risk should you appoint them to implement any of my recommendations.

Professional indemnity insurance doesn't work this way – it doesn't "shield" you from financial risk. The insurer only pays if you sue Cotswold Barristers, and win (with the insurer taking over the defence of the claim).

Insurance lawyers and underwriters we have spoken to are doubful their cover is £10m **per client** - it is probably £10m per claim, and if 500 clients sue Cotswold Barristers for the same mistake, that is usually one claim**. Dan talks more about these issues here.**

Summary

This opinion does not cover the most serious problem with the Property 118 structure.

Our report set out in detail why declaring a trust over rental properties, without the consent of the mortgage lender (or even telling them) in our view likely defaults the landlord's mortgage.

More importantly than our view is the view of UK Finance, the representative body for mortgage lenders:

> *"If someone wishes to transfer ownership of a buy to let property they should contact their lender to discuss whether this is permitted under the terms of any mortgage on the property. Transferring ownership of a property into a trust without informing your lender and seeking their consent would most likely be a breach of a mortgage's terms and conditions."*

Property118 refused to answer this point. The KC does not provide any view on the point – which is again fair enough, as it's not a tax point. However she does provide a clear warning:

> *"Implementation of the IS (without consents and so on) could mean that mortgagors are in breach of their obligations to their respective mortgagees but that would not prevent the necessary transfers of assets taking place for CGT purposes.* ***The situation concerning breaches of mortgage and insurance terms would be case specific and we cannot comment further on this point****.* [our emphasis]*"*

It's worth repeating this: Property118 are selling a structure which the mortgage lenders say is likely to default your mortgage, the KC acknowledges the point but doesn't provide a view on it, and Property118 have no response.

The elephant in the room

Why use the Property118 structure, and declare an unusual trust over your rental properties in favour of a company? What purpose and benefits does that have?

Tax.

There are lots of other benefits that you'd normally get by incorporating a property business. Most importantly, you segregate assets and liabilities. It also "looks" more professional (not a small point), and enables you to access some financial products that individuals can't. None of these benefits apply to the Property118 structure, because the wider world only sees the landlord. The trust and the company is invisible.

This means that a tax adviser would say that the structure has, as one of its main purposes (and main benefits), the obtaining of a tax advantage. The term many people would use is "tax avoidance".

This has consequences. It probably renders the structure disclosable to HMRC under DOTAS. It brings a panoply of anti-avoidance rules into play.

Tax advisers advising on entirely commercial deals, with no avoidance element, usually provide a detailed analysis of tax avoidance rules and principles. This opinion, on a scheme that has been accused of tax avoidance, doesn't even mention them.

In fact, the KC opinion summary doesn't once refer to "tax avoidance", "main purpose" or "main benefit". We doubt she missed the point. We expect she either wasn't asked the question, or was instructed to assume there was no tax avoidance.

This means the opinion is worthless.

DOTAS

Given the obvious tax main benefit/purpose, the high fees, and the claim the structure involves “valuable intellectual property”, we said that “it seemed likely” DOTAS applies. That remains our view.

The KC does not mention DOTAS. We can only assume she was asked not to.

DOTAS is important to Property118 – failure to disclose a notifiable scheme can result in penalties of up to £1m. It is also critical to their clients – if a notifiable scheme is not disclosed then HMRC has 20 years to go back and re-open the clients’ tax affairs.

Incorporation of an Unincorporated Business

4. When an unincorporated business is transferred by its owners to a company in return for an issue of shares in the company, save for unusual (possibly, exceptional) circumstances, that transaction will be of a capital character and, for tax purposes, will involve a disposal for consideration.

5. The primary tax which needs to be addressed in this context is capital gains tax (“CGT”), because the disposal referred to in the preceding paragraph, will in the absence of any exemption or relief, usually lead to a liability to CGT. The computation of the gain will, in a typical case (without exemption or relief), require the market value of the business disposed of to be treated as disposal proceeds, with the amount deductible being the historic cost of the assets which together comprise the assets of the business.

6. Section 162 Taxation of Chargeable Tax Act 1992 (“TCGA 1992”) provides a form of relief from liabilities to CGT that would otherwise arise on

incorporation of an unincorporated business. The relief takes the form of a rollover relief.

7. If interests in real property are transferred as part of the transfer of the business (including its assets) to a company, the charging provisions and reliefs relating to stamp duty land tax (SDLT) also need to be carefully addressed.

8. The transfer of the business will have some income tax and corporation tax implications (which often drive the desire to incorporate): these also need to be addressed when incorporating a business.

9. Other taxes such as inheritance tax ("IHT") must be considered as part of the overall tax evaluation; but IHT is unlikely to give rise to difficulties in straightforward cases on the basis that the incorporation of an unincorporated business will not involve any transfer of ultimate ownership (whether of the whole or part of the business concerned) and hence no transfers of value (which are key to the application of IHT).

10. More specific IHT planning has been considered, and possibly implemented, as part of more complex arrangements for some of the Advisors' clients. We understand that this planning has involved the creation of special classes of shares in so-called "smart companies".

11. Value added tax ("VAT") can be an important consideration in incorporations of businesses. Generally, it is important to ensure that the business is transferred "as a going concern" (in order to engage relevant relieving provisions). In the case of businesses whose activities are limited to letting residential property, VAT is usually of limited significance. VAT has not been mentioned by DN and we do not address it in detail in this Advice.

12. A number of commercial considerations arise in relation to incorporation of a business. These will vary on a case by case basis and we do not comment further on these.

The above is all uncontroversial.

Capital Gains Tax

13. In summary our view is that the incorporation strategy ("IS") offered by the Advisors (if properly implemented) does engage the provisions of s.162 TCGA 1992.

"If properly implemented" is important. Many tax schemes have failed because they weren't properly implemented. The KC was not asked to review implementation. We know neither Property118 nor Cotswold Barristers have any staff with tax qualifications. So who does ensure "proper implementation"?

14. We consider that DN's points concerning s.28 TCGA 1992 are correct.

Section 28 TCGA 1992 does not assist in determining whether the requirements of s.162 TCGA 1992 are satisfied. The function of s.28 TCGA

1992 is to determine the date of a disposal for CGT purposes but does not deem there to be a disposal nor does it identify what assets may have disposed of. The matter of whether there has been a transfer for the purposes of s.162 TCGA 1992 is a separate matter.

The “section 28” point was Mark Smith’s explanation of why the structure worked. We said it was wrong. The KC also thinks Smith is wrong.

15. On the other hand, s.28 TCGA 1992 does not mean that the requirements of s.162 TCGA 1992 cannot be satisfied.

We don’t know what this means. Why would anyone think s28 means the requirements of s162 can’t be satisfied? Perhaps there was something in the instructions on this?

16. We note that CGT applies primarily by reference to beneficial interests and to disposals thereof. A transfer is one form of effecting a disposal for CGT purposes. HMRC agrees with this. We refer to CG12700, CG12702 and s.60 TCGA 1992.

We said there was "considerable doubt" that s162 incorporation relief applies, because that requires the whole of a business to be transferred to a company as a going concern, and the absence of legal title in our view means that the business the company acquires is different from the original business. We didn't say we were certain on this point, and some advisers may take a different view (although our team was unanimous).

17. We do not consider that a transfer of legal title is required in order to engage the provisions of s.162 TCGA 1992. We refer to the case of *Gordon v IRC* [1991] STC 178 in which (whilst involving principles of Scots land law) the Court of Session held that “(3) Since the effect of what had been agreed between the partnership and N had been to put N [a transferee company] into the identical position previously enjoyed by the partnership, 'the whole assets of the business' had been transferred by the partnership to N, without the need for any conveyance to N of any real right of property in the estate.”

Here the KC is making a general point that is not relevant to the Property118 structure.

Gordon was a case involving a farming business. The land was ancillary to the business. The business was unaffected by whether the land was held directly, or though through a Scots law arrangement somewhat akin to a trust. For a property rental business, everything is different if you are merely the beneficiary of a trust, as opposed to the owner of the entire title.

For example: if you don't have legal title you can't raise finance. You can't liaise

with the existing lender. You also can't deal with tenants, lettings agencies and other third parties who aren't aware of the company's existence. Commercially and practically, it's not the same business. This is particularly the case if the trust has put the mortgage into default.

18. As we understand things, the IS involves a declaration of a bare trust over the legal titles to land. We do not consider that, for CGT purposes (where the ownership of beneficial interests in assets is key), the failure to transfer legal title at early stages in transactions means that the provisions of s.162 TCGA 1992 cannot be complied with. We do not consider that the holding of legal title (particularly in the context of the declaration of trust) means that anything can be said to have been left behind in the partnerships.

I'd probably agree with that. However, this isn't a "failure to transfer legal title at early stages". This is a trust that will remain in place for (in most cases) years, and legal title **cannot** be transferred during this time (because the mortgage will prevent it). The factors we list above therefore mean that the business the company is taking over is in practical and commercial terms different to the business the landlord previously carried on.

To just focus on the assets is the incorrect approach. s162 requires us to also focus on the business – did it transfer as a going concern?

It's not clear the KC understood the structure. Perhaps her instructions suggested the trust only existed for a short time? In fact it exists for at least as long as the term of the existing mortgage. Given the benefit of the structure is that landlords (supposedly) can refinance without disclosing the existence of the trust, it could remain in place for much longer.

19. We do not consider that considerations relating to mortgages and buildings' insurance affects the analysis concerning s.162 TCGA 1992. Implementation of the IS (without consents and so on) could mean that mortgagors are in breach of their obligations to their respective mortgagees but that would not prevent the necessary transfers of assets taking place for CGT purposes. The situation concerning breaches of mortgage and insurance terms would be case specific and we cannot comment further on this point.

As noted above, the question of whether the mortgage terms are breached, and the mortgage goes into default, is probably the most important point for Property118's clients, and neither Property118 nor the KC provides any assurance.

The KC was presumably not asked to consider the tax implications if the trust breaches the mortgage. This could include:

1. Is the trust effective if it breaches the mortgage, and does the company end up with beneficial ownership. Probably it does, per the *Don King* case. The analysis may well be easier given that here the prohibition on transfer is in a collateral contract (the mortgage) and not the property being transferred (the interest in land). However, this needs a full analysis. Where is it? Property118 certainly haven't undertaken it.

2. If we're right and beneficial ownership does move to the company, does the breach of contract prevent the company ever calling for legal title? The point is arguably academic given that the lender's security prevents legal title moving in any event, but it may nevertheless be relevant to the CGT analysis. Where is the analysis on this?
3. If the mortgage terms were breached, is the business still a "going concern" or does this point alone break s162?
4. It adds to the artificiality of the structure, given its central element necessarily involves a breach of contract to a third party (and in some circumstances potentially mortgage fraud).
5. We are aware of one case where it was successfully argued that a purported trust that breached the terms of a mortgage was a sham. Unusually, it was the **taxpayer** who ran that argument, in order to escape from the disastrous tax position that the trust structure had created. Where is the sham analysis?

20. We agree with DN on the need for there to be a "business" and the nuances that this can involve, it appears that the Advisors are alert to this point (which is a very real one) and apply case law on a case by case basis as well as related HMRC guidance on the need for sufficient activity.

Who are the personnel at Property118 and Cotswold Barristers who are qualified to assess the caselaw and apply it to the facts? It is not clear there are any.

The assumption of liabilities

21. In order for the conditions of s.162 TCGA to be met, there must be the transfer of the whole of the assets of a business (though cash does not need to be transferred). The only consideration for the transfer of the business to the company in relation to which the rollover relief given by s.162 TCGA 1992 can be secured is the issue of shares in the transferee company.

22. It is not unusual for liabilities of a business to be taken over by the transferee company on the incorporation of a previously unincorporated business. The assumption of liabilities could, without more, limit the application of s.162 TCGA 1992 because it will usually amount to the giving of consideration other than shares by the transferee company. HMRC's extra statutory concession ("ESC") D32 is relevant where liabilities are taken over by the company.

This is all agreed. We also noted that the assumption of obligations meant P118 were relying on ESC D32. The problem is that ESC D32 carries this warning:

> *"The general caveat that a concession will not be given in any case where an attempt is made to use it for tax avoidance should be borne in mind."*

The KC doesn't mention this point, although we are sure she is aware that ESCs cannot be used for tax avoidance purposes. Again, we suspect it's because she was asked to assume there is no tax avoidance in the structure.

23. The assumption (by the company) of liabilities to pay the monies due under the mortgage is expressly accepted by HMRC in ESC D32 as *not* giving rise to what we will describe as impermissible consideration for the purposes of s.162 TCGA 1992 and, accordingly, should not (of itself) adversely impact on the availability of the full relief provided by s.162 TCGA 1992.

What does "of itself" mean here? Is it a reference to tax avoidance?

24. We do not consider that the mortgage payments made by transferee companies have the character of income in the hands of the former partners. They will not be "interest" properly so-called and will not be miscellaneous income: and, accordingly, they cannot be chargeable to income tax under these two heads (which seem to us to be the only potential heads of charge).

The landlord is still paying the mortgage lender, and supposedly being compensated for this by the company. What is the payment from the company to the landlord?

We gave several possibilities in our paper: it could be capital (hence potentially non-taxable for the landlord, but non-deductible for the company). It could be income, taxable for the landlord as "annual payments"[1] or as "miscellaneous income". Another possibility: the company is settling a liability of its director, the landlord. Does that give rise to a charge under the benefit in kind (BIK), earnings or

[1] (On reflection we may have missed a point here. If "annual payments" (which is possible), the company has an obligation to deduct tax at 20%. That is creditable for the landlord, and so doesn't change the overall position, but does complicate it.)

distribution rules?

The KC says it's not income, which presumably means she thinks it's capital.

If that's right, this seems a very bad outcome for the client, because it means there is no deduction for the company, and the whole "section 24" planning fails. You can't have your cake and eat it. If capital for the landlord, it will surely be non-deductible for the company (e.g. because it's a payment of deferred consideration for the sale).

Or if it's not capital, why wouldn't it be taxable? The payment has many characteristics of an "annual payment" (it would seem to be "pure income profit" within *Conservators of Epping Forest*), and the scope of the miscellaneous income rule is very wide (e.g. given the continuing relevance of the old 19th century Schedule D Case VI caselaw such as *Attorney-General v Black*).

We would be surprised if the KC is "cakeist" who thinks the company has a deductible payment but the landlord has a non-deductible receipt. Perhaps we are missing part of her analysis?

The problem is that any result other than "cakeism" means the "section 24" planning fails, with all the potential scenarios resulting in a **worse** tax position than if the structure had not been put in place.

25. We agree with DN that there is no basis on which individuals can deduct mortgage payments for tax purposes once they have disposed of the related business.

26. The liabilities under the mortgages are not assets for CGT purposes and cannot *independently* be disposed within the scope of CGT (which applies to disposals or deemed disposals of "assets"- s.1(1) TCGA 1992): accordingly, no liabilities to CGT can arise from either the agreement on the part of the company to assume liability for the mortgage payments or from the receipt of individual mortgage payments by the individuals as a result of "disposal" of the liabilities under the mortgage. Any liability which would arise (in the absence of ESC D32) would result from the proportionate reduction in the amount of gain which is available for relief under s.162 TCGA 1992. See also paragraphs 35-37 below.

We don't understand this. Did the instructions really ask whether there could be a CGT disposal of mortgage liabilities?

(in the capital scenario, each payment by the company to the landlord would be a payment of deferred purchase price for the **properties**, and therefore potentially a CGT event)

SDLT

27. In summary, our view is that the incorporation of a partnership can be achieved without any charge to SDLT where the partners are connected with other for SDLT purposes.

28. We understand the points which DN makes in relation to circumstances where the necessary SDLT reliefs may not be available or where s.75A FA 2003 might apply; but we understand that fact specific analyses are carried out before the strategy is recommended to clients to ensure that the SDLT position is robust.

The KC was presumably not asked to express a view on this.

The SDLT position is entirely dependent on the legal position: ie, whether or not there is a partnership, which we discuss below.

The KC appears to have been told that "fact specific analyses are carried out" but we again, do not see who at Property118 or Cotswold Barristers has the expertise to look into this very specialised point. Users of the scheme may wish to test this, and ask Property118 to see the analysis carried out in their specific case.

The scope and application of the SDLT anti-avoidance provision, s75A, to the strategy is a difficult question. Unlike the legal issue of whether there is a partnership, this isn't sensitive to facts and should have been considered by the KC. Again, we would speculate that the absence of any consideration of anti-avoidance provisions was a requirement of the instructions.

29. The complex provisions of Schedule 15 Finance Act 2003 ("FA 2003") must be considered in each case, but, because most of the partnerships appear to be husband and wife partnerships, these provisions should not usually be in issue, given the way in which the formulae in paragraphs 18-22 Schedule 15 FA 2003 operate.

30. DN has made a point to the effect that a partnership might be retrospectively declared in order to be in a position to take advantage of s.162 TCGA 1992 and the SDLT relieving provisions.

31. It is our understanding that the Advisors look to determine if a business has, in fact and law, been operating as a partnership for some time and should properly be characterised as having done so rather than deciding that the proprietors can retrospectively declare a partnership. This is a question of fact and we cannot comment more specifically at this stage.

We said that Property118's practice was to claim that, in many cases where a husband and wife run a property rental business together, in fact they've always been a partnership, and partnership relief is available. They do this, even in cases where there was no partnership agreement, no partnership tax returns, and no extraneous evidence of any kind that a partnership existed.

We said it would only be in rare cases that this strategy succeeds, and SDLT relief applies - and HMRC guidance suggests that HMRC are likely to contest the point. The fundamental problem is that relations between a married couple are very different from relations between members of a business partnership.

The KC isn't disagreeing with any of that; she's just saying it's a question of fact.

The SDLT analysis depends entirely on the existence of a partnership. It's hard-edged (all or nothing). An SDLT liability based on 100 per cent of the value of the properties would arise if a partnership does not exist as a matter of law, and none exists if it does.

Clients should be concerned that (given no SDLT return is filed, and no DOTAS discloseure is made) HMRC have 20 years to interrogate the facts and issue assessments to impose SDLT, interest and penalties. Clients may wish to ask Property118 for full details of the legal analysis performed to confirm the existence of a partnership in their case. As noted above, we are doubtful Property118 has the capability to undertake this analysis.

VAT

32. We do not consider that we need to analyse the VAT position given that, as we understand matters, the transactions involved residential properties.

Corporation Tax

33. As regards the corporate entities, the express provision in s.330A(4) Corporation Tax Act 2009 ("CTA 2009") appears to permit a loan relationship debit for a corporate entity provided that the accounting requirements of s.330A(1) CTA 2009 are met.

Property118 have said the interest payments are deductible by the company "in accordance with normal corporation tax principles". That is not correct, because the company does not have a "loan relationship".

The KC agrees with us, and so has to look to the more exotic territory of s330A. She then gives a very weak view ("it appears to permit") which is correct, but entirely non-specific.

We mentioned s330A in our report, and said we doubted it would apply, because it is cashflows not risk that is transferred (as opposed, for example, to a sub participation or total return swap).

The KC does not appear to have considered this point; we do not know why.

We added that, even if s330A applied, given that the main purposes of the arrangement are to enable the Company to obtain a tax advantage; on that basis, s455C would apply to deny the deduction.

The KC does not address these points (consistent with the general approach of never mentioning the possibility of tax avoidance). Why?

The loan relationship analysis needs further consideration. What is the accounting treatment? What about s441? What about s444? There is no sign anyone has looked into any of this.

We have seen opinions on s330A in different contexts, and they run to 20 pages of dense analysis. It appears that all Property118 and Cotswold Barristers have done to date is assume interest payments are deductible by the company "in accordance with normal corporation tax principles". That is entirely inadequate, and it seems the KC agrees.

Refinancing

34. As we understand matters, the possibility of extracting capital from a partnership pre-incorporation and lending the funds to the company relies, as a starting point, on the basic principle that a taxpayer can extract capital from a business and replace it with borrowings as explained in HMRC's Manuals at BIM45700 et seq[1].

[1] We note that extracting capital prior to an incorporation is recommended as a commercial step in Simon's Taxes as follows: "If there is a substantial capital account in the unincorporated business, the business owner(s) should be advised to draw this down before incorporation, otherwise that capital will

35. We do not consider that refinancing involves any value shifting.

It is not clear from this that the KC has seen the details of the Property118 refinancing structure (which they described to a client as an "amazing opportunity").

The structure involves a two-week bridge loan with no purpose other than to gain a tax benefit (we mentioned it in passing in our original article, but subsequently received more details on how the structure works). There is no extraction of capital; it's a series of artificial steps which facilitate a subsequent tax-free extraction of capital. It is, in other words, tax avoidance. It's disclosable under DOTAS. We can't imagine HMRC would accept it.

The KC repeated the irrelevant HMRC manuals reference which Property118 use to justify the scheme, which adds to our impression that she was not presented with the actual structure.

The KC also refers to Simon's Taxes in the footnotes. Simon's is citing the example of the cash-rich business; allowing business owners to draw down the cash. It does not refer to artificially enhancing borrowings as a means of 'raising' capital. Again, the KC may not appreciate precisely what's going on here.

36. The analysis of the refinancing depends on the process followed in each case. Generally, we understand that whereas refinancing has not been a concern with HMRC, more recently HMRC may suggest that the liabilities which are taken over by the company in connection with refinancing are personal liabilities and are not liabilities of the business.

In this case it is clear that the bridge loan liability taken over by the company was a personal liability of the landlord, and not a liability of the business. It wasn't used for the business, and had nothing to do with the business. It only existed for two weeks, and sat in a solicitor's client account throughout. The KC appears to have been given wrong facts.

37. Where business liabilities are assumed by a company as part of the IS following refinancing and remain business liabilities, ESC D32 should continue to apply.

Unless there is avoidance, in which case it won't.

IHT

38. The use of family investment companies, or "FICs", as succession planning vehicles is fairly standard planning nowadays; and it is indeed possible to create shares which have no or very little initial value[2]. It all depends on the terms of the shares as defined by the Articles of Association (possibly read with related shareholders' agreements). Valuation is not an exact science and judgements will have to be made in individual cases: but there are standard

ways of valuing companies and the valuation of non-trading or investment entities is usually regarded as more straightforward than valuation in many other scenarios.

This is, again, a very weak statement. To say something is “possible” is hardly supportive.

We are aware that FICs are sometimes created with shares that are entitled to all capital growth past the point where a “hurdle” is reached, for example once the company’s value has grown by 20%. Property118 don’t use a hurdle. Our specialists (familiar with FICs) thought it was clear such shares would have immediate value. One eminent adviser we spoke to had recently litigated a case where shares of this type were in fact found to be worth a seven-figure sum.

So the problem is that Property118’s planning does not appear to be in line with the “standard planning” to which the KC refers.

The KC may not have been given the information on how the shares were structured. If she had, we’d expect her to state a view, even if only a tentative one. The terms of the shares are simple, and we believe all Property118’s structures follow the same approach.

Fortunately, there is an easy way to settle this matter, and for Property118 to prove the shares have zero value. Tax Policy Associates will gladly pay £10 for them (subject to contract). If they truly have zero value, then the owners should be delighted at that offer. We will then happily agree that was the correct value. Why not?

(The answer is: because the shares have a good chance of becoming very valuable, with zero downside risk. Which is why they have value today, and why nobody’s going to sell them for a tenner)

There are two further IHT-related points the KC does not mention:

The sham trust

We’ve seen Property118 recommend the “Creation of a Discretionary Trust controlled by you via a Letter of Wishes to shelter all future capital growth in the portfolio from Inheritance Tax”. A trust “controlled by you” isn’t a trust – it’s a sham (and not protected from IHT).

The KC does not address this – we expect because Property118 know it’s indefensible, and didn’t put the point to her.

Diverting income to children

The Property118 structure involves creating shares for children, so they can receive dividends and pay less tax than the parents (because of their allowances and lower tax rates). But there are specific rules that stop this.

The KC doesn't address the point, probably for the same reason.

Enquiries

39. We have seen some enquiry correspondence with HMRC in which HMRC's questions appear to have been properly answered with documentation provided where requested.

This is a very specific answer, suggesting the KC saw only very limited documentation.

We continue to believe that the structure has never been fully disclosed to HMRC. We also doubt the claim from Property118 that "HMRC has confirmed [our] strategy is perfectly above board"

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02 October 2023

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be locked into the value of the shares." There is no suggestion that this is an improper or risky course of action.

[2] IHT planning based on low initial share values is not a new concept. In addition, a lot of planning (and legislation) in the employment related securities arena has been based on shares with low initial values.