MAIN RESIDENCE RELIEF – THE TWO-YEAR TIME LIMIT REVISITED

Keith M Gordon[1]

The High Court case of *Griffin (Inspector of Taxes) v Craig-Harvey*[2] is generally accepted as authority for the rule that taxpayers with more than one residence must elect which is to be their main residence within two years of acquiring a second (or further) residence (or within two years of ceasing to have a residence). Once such an election is made (and within the two-year time frame), taxpayers are then free to make further elections at any time which may then be backdated by up to two years. The effect of this rule can be demonstrated by an example.

1 Example of the rule in *Griffin v Craig-Harvey*

Suppose Scott owns a home in Chelsea. On 1st March 2004, he acquires a second home in Cambridge which he plans to use each weekend. Assume that both properties are used by Scott as his residences.

Scott is therefore entitled to elect for capital gains tax purposes which of the homes is to be his main residence. Such an election, according to *Griffin v Craig-Harvey* must be made by 28th February 2006.

Once Scott makes such an election he can vary it at will and effectively backdate such a variation by up to two years. So, for example, Scott could make an election on 25th March 2010 and backdate it to 25th March 2008. However, if Scott had not made the initial election within the two year-period, no election may be made at all (unless a third residence were ever acquired).

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2 [1994] STC 54

2 The legislative provisions

Such elections are provided for in section 222(5) of the Taxation of Chargeable Gains Act 1992. That subsection (as amended) reads as follows:

> (5) So far as it is necessary for the purposes of this section to determine which of 2 or more residences is an individual's main residence for any period–
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> > (a) the individual may conclude that question by notice to an officer of the Board given within 2 years from the beginning of that period but subject to a right to vary that notice by a further notice to an officer of the Board as respects any period beginning not earlier than 2 years before the giving of the further notice.

Paragraph (b) of that subsection and the words following it were repealed by the Finance Act 1996, section 134 and Schedule 20, paragraph 59(3)(a).

Paragraph (a) refers to an election which must be made "within 2 years from the beginning of [a] period". In this article, I shall call this an "initial election". Any election to vary the terms of an initial election shall be referred to as a "subsequent election".

3 Mr Craig-Harvey's contentions

Mr Craig-Harvey was arguing that an initial election may be made at any time, subject to the rule that its effect may only be backdated by up to two years. In other words, Mr Craig-Harvey argued, an initial election works in much the same way as any subsequent election.

Whilst the Special Commissioner upheld Mr Craig-Harvey's appeal, Vinelott J disagreed and held that initial elections must be made within two years of a taxpayer acquiring (or disposing of) a residence and that failure to make a timely initial election would preclude a taxpayer from making a subsequent election.

What remains of section 222(5) makes no mention of a taxpayer's acquisition or disposal of a residence and it is difficult to see how the Court could have reached such a conclusion. However, it is important to realise that Vinelott J was looking at the previous incarnation of the rule (in section 101(5) of the Capital Gains Tax Act 1979).

4 Section 101(5) of the Capital Gains Tax Act 1979

The disposals made by Mr Craig-Harvey were fully dealt with by the Capital Gains Tax Act 1979. The equivalent provision to section 222(5) was section 101(5) which read as follows:

> (5) So far as it is necessary for the purposes of this section to determine which of two or more residences is an individual's main residence for any period–
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> (a) the individual may conclude that question by notice in writing to the inspector given within two years from the beginning of that period, or given by the end of the year 1966-67, if that is later, but subject to a right to vary that notice by a further notice in writing to the inspector as respects any period beginning not earlier than two years before the giving of the further notice,
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> (b) subject to paragraph (a) above, the question shall be concluded by the determination of the inspector, which may be as respects either the whole or specified parts of the period of ownership in question,
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> and notice of any determination of the inspector under paragraph (b) above shall be given to the individual who may appeal to the General Commissioners or the Special Commissioners against that determination within thirty days of service of the notice.

There are two substantive differences from the text as it now stands.

First, paragraph (b) and the words following it were then present. These words were repealed as part of the transition to Self-Assessment in 1996/97 as it was felt that reliance upon the Inland Revenue's determination of any issue was not in keeping with the principles of Self-Assessment.

Secondly, in paragraph (a), the 1979 statute allowed initial elections to be made

> *"by the end of the year 1966-67, if that is later [than the end of the period to which the election relates]".*

That provision was relocated to TCGA 1992, Schedule 11, paragraph 19 when the legislation was consolidated in 1992.

These two differences featured in Vinelott J's reasoning. Consequently, this article considers these differences and discusses whether the changes made since 1979 are so significant as to render doubtful the continuing relevance of the decision in *Griffin v Craig-Harvey*.

5 Former paragraph (b)

Vinelott J held (in my view correctly) that the provisions of paragraph (a) are "in substance an exception from the general rule set out in para. (b)". In other words, it was (prior to the introduction of Self Assessment) the inspector who concluded any debate about which of two residences was the main residence, but an inspector's determination could be trumped by that of the taxpayer.

The question that is then asked is whether the repeal of this paragraph in 1996 impacts upon the interpretation of paragraph (a) which was left unamended.

The normal rule of statutory interpretation is that the meaning of what is left of a statutory provision is not intended to change when part of the provision is repealed.[3] Consequently, that would suggest that the meaning of paragraph (a) did not change merely by the repeal of paragraph (b) and the closing words of the subsection. The rule in *Attorney General v Lamplough*, as ever, is subject to the amending Act indicating a contrary intention.

The amending provisions in FA 1996 do not, in my opinion, indicate any such contrary intention.[4]

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3 *Attorney General v Lamplough* (1878) 3 Ex D 214 (Court of Appeal). That case concerned the meaning of the tail words in a list after certain items of the list were repealed. It was held that a product which had been manufactured and sold by the defendant was covered by the words in the list as originally enacted. Consequently, the product did not fall within the sweep-up provisions in the tail. The repeal of certain items in the list did not, it was held, have the effect of bringing the product within the scope of the tail.

4 The actual provision reads as follows:

> In subsection (5) (determination of individual's main residence)–
> (a) paragraph (b) (which, subject to conclusive notice by the individual under paragraph (a), provides for the question to be determined by an inspector), and
> (b) the words following that paragraph (right of appeal against inspector's determination), shall cease to have effect (Finance Act 1996, Schedule 20, paragraph 59(3)).

But did the learned Judge actually reach the right conclusion with regards to the meaning of paragraph (b)? Having explained that paragraph (b) was setting out the "general rule" to which paragraph (a) represented the exception, he continued:

> *"In this context the reference to 'any period' in the opening part of s. 101(5) and to 'that period' in para. (a) are most naturally read as referring to 'the whole or any part of the period of ownership in question' that being the period in relation to which in default of agreement or of any notice under para. (a) the inspector's determination is to be made."*

Whilst following the Judge's train of thought requires an element of linguistic acrobatics, I would suggest that there is nothing too controversial in these words. However, I cannot see how this reasoning (assuming it to be correct) supports the conclusion that the Judge then reached.

Having aligned the early references to "any period" and "that period" to the words "the whole or any part of the period of ownership in question" in paragraph (b), the Judge appears to have focused on the words "the period of ownership in question" without regard to the immediately preceding words referring to "the whole or any part of [that period]".

It is therefore my view that these early references to "any period" and "that period" can refer to "any part of the period of ownership" just as much as the whole of the period of ownership. Consequently, it would follow that an election by the taxpayer (under paragraph (a)) can properly be made with effect from a time other than the beginning of the period of ownership and therefore need not be made within two years of any change in circumstance.

6 The reference to 1966-67

However, the Judge said that his interpretation of what was then section 101(5) was reinforced by the presence of the words "or given by the end of the year 1966-67, if that is later". In the Judge's view:

> *"The draftsman … clearly had in mind the possibility that the period of two years from the beginning of a period of ownership of two or more residences might have expired before or have been current when the Finance Act 1965 (from which these provisions are derived) came into force."*

It should be noted that section 101(5) reproduced *verbatim* the provisions of section 29(7) of the Finance Act 1965.

Once again, I cannot quibble with the Judge's analysis. However, I would respectfully express disagreement with the conclusion he reached.

The judgment is silent on the matter, but one must suppose that the Judge was working on the basis that the status of the property prior to 6th April 1965 had no effect on the calculation of main residence relief.[5] Such a conclusion would, initially, be supported by Finance Act 1965, section 29(13)(b) which read as follows:

> *"[Period of ownership] for the purposes of subsections (2), (3) and (4) of this section, shall not include any period before 6th April 1965."*

Consequently, section 29(2) (of the Finance Act 1965) would have exempted the whole of any gain arising in respect of a residence that was an individual's main residence throughout the period from 6th April 1965 notwithstanding the status of the property before that date. Conversely, section 29(3) would not have permitted any exemption in respect of a residence sold on 10th April 1965 (say) which had ceased to be the individual's main residence a week earlier after having been the individual's only home for the previous twenty years.[6]

It would appear that Vinelott J recognised that a taxpayer in this latter situation might have wished to make an election in respect of the property so that it would have been treated as the individual's main residence for the whole of the period of ownership and, in particular, for the entire period of ownership falling after 5 April 1965.

Consequently, there was a reason to make elections in respect of residences whose periods of ownership commenced before 6th April 1965. And, so as to reflect the two-year timeframe generally permitted by the section, it was necessary to provide that such elections could be made any time up to 5th April 1967.

However, it was not, in my opinion, necessary for a taxpayer to make any election in respect of any period after 5th April 1965 for main residence relief to

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5 This would be in the same way that the use of a residence before 31 March 1982 is not relevant under the current provisions (TCGA 1992, section 223(7)) – something that can work both in favour of, and against, taxpayers.

6 The transitional rules in Finance Act 1965, Schedule 6 would in such a case, however, had limited the gain to that proportion arising after 5th April 1965.

apply.[7] Equally, it was not necessary for a taxpayer to make any election in respect of the ***whole of a period*** of ownership. And the limited scope of section 29(13)(b) clearly provides that references to "the period of ownership" in section 29(1) (say) apply as much to periods on or before 5th April 1965 as to periods after that date. Let us consider the following example.

Suppose, on 1st February 1960, an individual purchased three properties, Blackacre, Redacre and Whiteacre, all of which are occupied as residences. On 1st March 1962, Blackacre was let out under a four-year lease; the individual subsequently occupying Whiteacre and Redacre as residences.

On 1st March 1966, the individual sold Blackacre and Whiteacre (without having reoccupied Blackacre) and continued to live in Redacre. The individual would clearly try to minimise the gain arising, if not eliminate it altogether. On the other hand, suppose that the individual wanted Redacre to be his or her main residence with effect from 6th April 1965 so as not to risk losing any capital gains tax relief thereon.

Under the terms of what became section 101(5)(a) of the Capital Gains Tax Act 1979, a "subsequent" election could not apply to any period more than two years before the making of the election. Consequently, it would not have been possible for a subsequent election to have been made in respect of Blackacre, as it was not the individual's residence at any time during the two years before 6th April 1965 nor any time thereafter.

Consequently, if Vinelott J is correct, it would have been necessary for an ***initial*** election to apply to Blackacre if any gain arising therefrom is to be exempt from charge. Following the change in the situation in 1962, the Inland Revenue's practice would allow a further initial election to have been made in respect of Whiteacre – say, for some period during 1964. A subsequent election would then have been made in favour of Redacre in respect of the period following 5th April 1965. Both Whiteacre and Blackacre would then have been properties which "at any time in [the individual's] period of ownership ... his [or her] only or main residence" as required by section 29(1) of the Finance Act 1965. Whilst section 29(2) would not have applied because neither property was the main residence during any (let alone all) of the period of ownership falling after 5th April 1965, relief would still have been available under the terms of section 29(3). In both cases, the entire period after 5th April 1965 would have been exempted under

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7 This is because elections cover the whole or part of any period of ownership (section 29(7)) and the meaning of "period of ownership" in section 29(7) was not restricted to periods post 5 April 1965 (section 29(13)(b)).

what was then the 12-month rule[8] even though the period the properties qualified as main residences fell before 6th April 1965.

Similarly, if Whiteacre had been let out from 1 March 1964, say, it would have been possible for a subsequent election to be made in respect of the period 1 January 1964 until 29th February 1964 in favour of that property. As a result, neither disposal would have given rise to any chargeable gain even though neither property had been occupied as residences after 5th April 1965.

Had, alternatively, both Blackacre and Whiteacre been let out from 1 March 1962 then, according to Vinelott J, the gain from only one of these could have been exempted from charge. That is because no subsequent election could have been made in respect of either property.

But, as mentioned above, section 29(7) considered determinations which could have been "as respects ***either the whole or specified parts*** of the period of ownership in question" (emphasis added).

It is my view that the legislation is saying that periods forming part of a period of ownership may be subject to an ***initial*** election – and subject to variation at any time (provided that such changes only go back at most two years). Thus in the last variant of the above example, it would have been totally in order for an ***initial*** election to have been made for the period between 1960 and 1961 (say) in respect of Blackacre and a further ***initial*** election in respect of Whiteacre for the period from 1961 to 1962. There would have been no need to vary such elections and therefore the two-year time limit for ***subsequent*** elections would not have been relevant. Since the provisions permitting such elections were not introduced until FA 1965, it was only right that the legislature should allow such elections to be made at any time until 5th April 1967.

It was for that reason, in my opinion, that the words "or given by the end of the year 1966-67, if that is later" were included.

The alternative would, in my opinion, be highly anomalous. Whilst anomalies are sometimes inevitable when interpreting taxing statutes[9], it is suggested that the anomalies highlighted above would not have been within the legislative intention. Consequently, it is my view that Vinelott J misunderstood the relevance of the backstop date of 5th April 1967 and that the ability for a taxpayer to make an initial election before that date in fact suggests that initial

8 currently 36 months (TCGA 1992, section 223)

9 In *Craig-Harvey* Vinelott J accepted that anomalous consequences might arise, but that these arise from the ability of taxpayers to make retrospective "subsequent" elections.

elections may be made at any time (subject only to a limit of two years' retrospection).

7 The subsequent omission of the reference to 1966-67

Even if I am wrong on the last point, it is arguable that Vinelott J's judgment is no longer authoritative.

When the Capital Gains Act 1979 was consolidated into the Taxation of Chargeable Gains Act 1992, the words "or given by the end of the year 1966-67, if that is later" were relocated to Schedule 11, paragraph 19.

Whilst the 1992 Act purported to be a straight consolidation[10], this relocation of certain provisions could be sufficient to allow the provisions to be considered afresh.[11] However, it is my view that the rearrangement of the text in this particular case would not be sufficient to sustain such an argument.[12]

8 *Pepper v Hart*

The final aspect of Vinelott J's judgment considered the Parliamentary statements which accompanied what became section 29(7) of the Finance Act 1965.

I am in agreement with the judge when he says that there is no ambiguity or obscurity in the provision, although I believe its meaning is significantly different from that inferred by the Judge.

Interestingly, what became section 29(7) was subject to an amendment and therefore the provision was subject to greater Parliamentary comment than might otherwise have been the case. As originally drafted, clause 28(7) (as it then was) read:

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10 Its long title read: "An Act to consolidate certain enactments relating to the taxation of chargeable gains."

11 See, for example, Dillon LJ in *Pocock v Steel* [1985] 1 WLR 229 at 233E.

12 That has been described as a 'fraud on Parliament'. See, for example, Bennion, *Solicitors' Journal*, 'A Point on the Companies Consolidation', 130 SJ (1986) 736.

> (7) So far as it is necessary for the purposes of this section to determine which of two [or more][13] residences is an individual's main residence–
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> (a) the individual may conclude that question by notice in writing to the inspector given within two years from the date of the acquisition of, or of his original interest in, the dwelling-house which is treated by the notice as his main residence, or given by the end of the year 1966-67, if that is later, but subject to a right to vary that notice by a further notice in writing to the inspector as respects any period beginning not earlier than two years before the giving of the further notice,
>
> (b) subject to paragraph (a) above, [the question][14] shall be concluded by the determination of the inspector, which may be as respects either the whole or specified parts of the period of ownership in question,
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> and notice of any determination of the inspector under paragraph (b) above shall be given to the individual who may appeal to the General Commissioners or the Special Commissioners against that determination within thirty days of service of the notice.

So, at that stage, the Parliamentary drafter was clearly envisaging initial elections being made during the two years after the acquisition of a property. But it quickly became apparent that the drafting was flawed and a more flexible approach was needed. Consequently, two amendments were made:

> (i) in the opening words, "for any period" was inserted after "main residence";
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> (ii) the words "beginning of that period" were substituted for "date of the acquisition of, or of his original interest in, the dwelling-house which is treated by the notice as his main residence.

It is my view that these amendments significantly changed the emphasis of the provision in a number of ways. First, the use of "that period" in the second of these amendments can be seen to correspond with the words "for any period" inserted by the first amendment. Thus, in itself, it indicates that the two-year

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13 These words were inserted by a previous amendment.

14 These words were inserted by a subsequent amendment.

election time limit runs from the beginning of any such period and not merely the date of an acquisition.

Secondly, the purpose of these amendments was to ensure that elections could be made in respect of a particular residence more than two years after that particular residence was acquired. As Mr Niall MacDermot, the Financial Secretary to the Treasury explained:

> *"Under subsection (7) [as originally drafted] there is no provision for the case of a man who has one house and does not need to make any option but who later buys another house and then wishes to opt to treat the other [i.e. the first] as his principal residence. The effect of this Amendment is to keep open the option so that he can exercise a choice within two years from the time when he acquires the second house."*[15]

Mr MacDermot's statement is perfectly correct. Where I am in respectful disagreement with Vinelott J, however, is that I would submit that the effect of the amendments is a little wider. Amending the Financial Secretary's words, I would assert that:

> The effect of this Amendment is to keep open the option. For example, so that a man can exercise a choice within two years from the time when he acquires a second house. ***Or later, if he so chooses.***

9 Disposals of residences etc

The above discussion has made the assumption that the disposal of a residence can trigger a new two-year window to make an initial election.[16] However, there is nothing in section 222(5) or its predecessors to suggest that this should be the case. Indeed, if Vinelott J is right, an initial election must be made (if at all) within two years of a residence being acquired. But this was based on the Judge focusing on the words "period of ownership". It seems incredible, if this analysis is correct, that a new period of ownership is deemed to commence on the disposal of another residence.

Similarly, the Judge's interpretation seems to focus on the period of ownership of a residence and not the period for which the property was used as a residence. So, supposing a property had been owned since 1985, but had been let out until

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15 *Hansard* 1964-65, Vol 713, Col 1002, 27th May 1965

16 This is the Inland Revenue's practice, see the Capital Gains Manual, paragraph CG64496.

2004 and only occupied as a residence of its owner at that stage, it would follow that (all other things being equal) the time to make an election would have expired by 1987 even though the property would not have been eligible for relief until nearly two decades later.[17]

Both of these situations are overcome by Revenue practice. However, in my view, these practices represent a fudge to make workable what is an incorrect interpretation of the law. A rolling two-year time limit does not give rise to such issues and is therefore a better indication of what Parliament would have intended when the provisions were introduced.

10 Conclusion

It is therefore my view that the better reading of what is now section 222(5) of the Taxation of Chargeable Gains Act 1992 allows main residence elections to be made at any time (but with a two-year limit on retrospection).

However, in view of the decision in *Griffin v Craig-Harvey* and the Inland Revenue's reliance upon that authority, I would continue to urge taxpayers to make protective elections within two years of each acquisition (and disposal, where appropriate) of a residence. Nevertheless, where a time limit has been missed, it is my view that, in a suitable case, it would be worth seeking to overturn the decision in *Griffin v Craig-Harvey*.

17 Again, in practice, the Inland Revenue would require an election to be made within two years of the property being occupied as a residence.