SECTION 776 INCOME AND CORPORATION TAXES ACT 1988

Adrian Shipwright[1]

Introduction

General

S.776 ICTA 1988 is a wide anti-avoidance section of uncertain ambit aimed at "development profits" not otherwise chargeable as income. The realisation of a gain indirectly through the sale of company shares, interests under a settlement or a partnership was held not to be a trading transaction in a number of cases. Hence what is now s.776 ICTA 1988 was enacted. The purpose of this article is to consider the meaning of the section and its impact in some of the more usual development circumstances.

Appendix I contains a summary of cases under s.776 ICTA 1988.
Appendix II is an outline of points to consider on s.776 ICTA 1988.

Scope of the Section

S.488 TA 1970[2] is sidenoted "Artificial Transactions in Land". However, it is wider in its scope than this (see e.g., Buckley L J in *Yuill v Wilson* [1979] STC 486 at 491) and interestingly s.776 ICTA 1988 is sidenoted "Transactions in land: Taxation of Capital Gains".

Although in the early years following its introduction the Revenue seemed not to use the section, this has now changed and anyone involved with land and development ignores the section at his peril even if he is not seeking to avoid tax.

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2 The original enactment of what is now s.776.

As will be demonstrated later the section can apply to much more than "Artificial Transactions" and may catch some purely commercial transactions. Often it will not catch an individual who makes a straight purchase with the object of realising a gain in one of the prescribed ways because the likelihood is that such an activity will be trading. This does not mean that the section cannot catch such transactions.

It should be remembered that s.776 ICTA 1988 covers both direct and indirect gains attributable to land. S.776 ICTA 1988 seems to be intended to look behind the legal form to the business reality of the section though this is nowhere spelt out in terms (cf s.739 ICTA 1988).

Its wide wording, though, does not seem to give it as wide a scope as its drafting would suggest (see below). Its application, however, can be capricious and can prove a trap for the unwary. The legislation is to be found not just in s.776 ICTA 1988 but in s.777 ICTA 1988 which supplements both s.775 and s.776. There is a wide power to obtain information set out in s.778 ICTA 1988.

The section applies not only to land but also to assets *deriving their value from land.* This would include shares in a land investment company. Presumably it would include also unit trusts such as a Single Property Unit Trust. The interest of a beneficiary under a trust is specifically included by s.776(13)(b) ICTA 1988.

Origins of S.776

S.776 ICTA 1988 was introduced in its present form in 1969. The origins of the section may help in understanding it and when it may apply. It and the earlier legislation in the 1960 and 1962 Finance Acts concerned stock stripping. Roy Jenkins was at his most helpful in his Budget speech when, introducing the provisions which became s.776, he said: "The Finance Bill will contain provisions to counter tax avoidance in three fields. The first relates to the profits arising from land where the provisions of ss.21-26 of the Finance Act 1960 have been found to be inadequate to deal with some of the devious schemes for avoiding charges on dealing although it is abundantly clear that dealing has in fact taken place." One might have thought that there would have been an easier approach than s.776, namely for the Revenue to argue that there was a trade. This was before the principle in *Furniss v Dawson* had "emerged" and so might have been a harder course then than now. However, a legislative approach was taken and what is now s.776 was introduced. It was also aimed at the sale of property deriving its value from land and this may explain the position. The sale of shares in a property owning company would normally only be a capital transaction (cf *Associated London Properties Ltd v Henriksen* (1944) 26 TC 46).

The drafting approach is to impose a charge in wide and general terms. This has been called by one commentator an "elephant gun" technique. He continued:

> "...the point of the description is that the Revenue appear to be uncertain what precisely the target is so they fire off an enormous gun in the general direction of where they suppose the target to be in the hope that they will hit something worthwhile. The inevitable result is that in the long grass many innocents may have ventured unwittingly into the target area and may get hit in addition to, or instead of, the intended target."

An apparent example of this is *Page v Lowther* infra.

Buckley L J said of reading the section "I confess that ... I travelled through the section finding very little light on the journey to aid my understanding of it".

It may be that cases of the *Ransom v Higgs* type (1974) 50 TC 1 were what the legislators had in mind. This was a complex series of transactions allowing profits to be realised indirectly (for a diagram of the transaction see [1980] BTR at page 468). Mr Higgs who had merely "procured" the actions of the trading actors was assessed on the profit arising under Schedule D, Case I. The House of Lords held he was not so assessable. Lord Wilberforce said:

> "... if schemes such as these succeed in taking trading stock profits - by a stripping process - outside the net, the remedy as in the case of dividend stripping lies in legislation. Indeed, if one asks for a description of what this scheme is, if it is not trading, the answer is to be found in the Finance Act 1969, s.32 - a section passed eight years after these transactions and so too late to catch them. It is (I take my words directly from the Section) an artificial transaction in land by which land held as trading stock is disposed of by an arrangement or scheme which enables a gain to be realised by an indirect method by a person who is a party to or concerned in the scheme...".

This at least is House of Lords' authority (albeit obiter) as to circumstances when the section will definitely apply.

Avoidance Requirement?

S.776 is found in Part XVII ICTA 1988 headed "Tax avoidance". One might have thought that an avoidance motive would be a necessary condition for the application of the section. This does not seem to be so. S.776(1) provides "This section is enacted to prevent the avoidance of tax by persons concerned with land or the development of land". The reason for, and the effect of, this preamble are uncertain. Although there are conflicting dicta in the case law it seems that no tax avoidance motive is necessary for the section to apply. In *Page v Lowther* [1983] STC 799 the provisions were applied to a transaction which was entered into which had no tax avoidance motive and which was most commercial in its design rather than an artificial transaction (see especially pages 805 and 808). It would therefore seem unsafe as a matter of law to rely on a defence that it was a *bona fide* commercial transaction, though in practice this will be an important factor in any clearance application or dispute with the Inland Revenue.

Areas Where the Section is likely to Apply

Introduction

It seems that there are three areas in particular where the section can apply. These are:

(a) passing on the profit to someone else;

(b) retention of a "slice of the action"; and

(c) an indirect realisation of a profit.

It may be that (a) and (c) are not particularly different.

These situations are the areas that are most likely to interest the tax planner so the impact of s.776 ICTA 1988 must always be borne in mind in any land transaction.

Passing on Profits to Another

The most recent case on this is *Sugarwhite v Budd* (see Appendix I). In this case a solicitor had arranged transactions by a Bahamian company. The taxpayer was found to be an active party to the arrangements under which the taxpayer had diverted capital to the Bahamian company. It was held that s.776 applied in the circumstances.

Other cases that fall in this heading include *Yuill v Wilson* (see Appendix I) and *Williams v Davis* and *Williams v Nesbet* 26 TC 371. The latter cases are an example of passing on a profit to a person not liable to tax on the profit. They involved gains realised by the wives of partners in a development business related to land given to them by their husbands. The land was sold to a company of which the husbands were directors and shareholders. The wives were not held to be trading and not liable to income tax. There was no CGT at the time.

The former case is an example of passing on the benefit to a non-resident outside the charge to UK tax. The Channel Island companies made the profit and did not pay tax on it. This offshore aspect is something that the Inland Revenue particularly dislike. The gain is then going entirely outside the UK tax net unless s.776 ICTA 1988 applies. It seems the Revenue in practice may be less ready to invoke s.776 ICTA 1988 if they will get the tax from someone else in the UK. This is not a matter of law but rather of convenience and should not be relied on.

"Slice of the Action"

The classic case illustrating this head is *Page v Lowther* (see Appendix I). The trustees in that case entered into sensible, seemingly commercial transactions to maximise the return to the settlement for the benefit of all the beneficiaries. There was no artificial transaction and no tax avoidance motive but it was held that the section nevertheless applied. It is not clear what the trustees' duty would be in such case now. Presumably to maximise the net of tax return.

Equally in *Winterton v Edwards* (see Appendix I) the employees only wanted their just deserts.

S.776 ICTA 1988 only seems applicable where it is a slice of the development profit that is obtained. Less difficulty is likely to arise where a slice of the land profit, before any development profit has arisen, is concerned.

Indirect Realisation of Gain

An example of this would be the transactions in *Ransom v Higgs* discussed above. Mr Higgs had procured that certain things happen but was not trading. Lord Wilberforce said such an indirect realisation would now fall within what is now s.776 ICTA 1988 (see supra).

A number of cases before the introduction of s.776 ICTA 1988 involved the indirect realisation of land value by selling shares in a company (see e.g., *Associated London Properties v Henriksen* (1944) 26 TC 46). These would now seem to be caught by the section.

Requirements for the Section to Apply?

General Requirements

In order for the section to apply a *gain of a capital nature* has to be obtained from the *disposal* of the *land*. In more detail the conditions are

(a) (i) that land or property deriving its value from land was acquired with the sole or main object of realising a gain from disposing of the land, etc; or

(ii) that land is held as trading stock; or

(iii) that land is developed with the sole or main object of realising a gain from disposing of the land when developed; and

(b) A gain of a capital nature is obtained from the disposal of the land; and

(c) (i) that gain is obtained by the person who acquired, held or developed the land or any connected person; or

(ii) a scheme or arrangement has been effected allowing a gain to be realised by an indirect method by any person who is a party to or concerned in the scheme or arrangement.

Gain for Another Person

It does not matter whether the person obtains the gain himself or for another person - a tax charge can still arise (see s.776(8) ICTA 1988). This would catch most trustees. Questions can arise as to whether a charity obtains a gain for "persons" rather than for a purpose. Equally "purpose" trusts of the *Re Dean* (1889) 41 ChD 552 type may not be for "persons". *Re Dean* concerned a purpose trust to maintain the trustees' horses and hounds. A purpose trust of the *Re Denley* [1968] 3 All ER 65 type would seem to be for persons. *Re Denley* concerned a sports ground primarily for the benefit of the employees of a particular company. These do not seem very hopeful vehicles for tax planning.

"Gains of a Capital Nature"

In simple terms, for s.776 ICTA 1988 to apply it is necessary that there be a transaction in land and a gain of a capital nature be derived.

In broad terms, a gain of a capital nature is any sum which does not fall to be included in a computation of income for the purposes of the Tax Acts (cf s.489(13) TA 1970 now s.777(13) ICTA 1988).

"Land is Disposed of"

By s.776(4) ICTA 1988 it is provided that land is disposed of if, by any one or more transactions, or by any arrangement or scheme, whether concerning the land or property deriving its value from land, the property in the land or control of the land is effectually disposed of. This is very wide in ambit.

"Development"

There is no definition of development for these purposes in the section. It is therefore to bear its natural meaning though the planning position may be a helpful guide when it is not too technical. The amount of development does not, it seems, need to be that great (see *Winterton v Edwards* [1980] STC 206). Alteration of an existing building may amount to development in some circumstances. A mere change of use would not be development for these purposes notwithstanding the planning permission position.

Effect of the Section Applying

Where the section applies a charge to tax arises under Schedule D Case VI (see s.776(3)(a) ICTA 1988). Schedule D Case VI is the "sweeper up" provision. It has some restrictive rules. It seems that s.776 ICTA 1988 cannot be used by the taxpayer to create an income rather than a capital loss though the author is not aware of

authority directly on this point.

Definitions

"Land"

For these purposes "Land" includes references to all or any part of the land and includes buildings and any estate or interest in land or buildings (s.776(13)(a) ICTA 1988).

Equitable as well as legal estates and interests are therefore included.

There is no specific requirement in the legislation that the land be in the United Kingdom. Subsection (13) is curiously worded and might suggest that only UK land is included but is not conclusive. It is believed, though, that the present practice of the Inland Revenue is to apply the section to UK land only.

Since the definition provides that land includes part of the land it is not necessary that the whole of the land be acquired or developed with a view to a gain on disposal for the section to apply. S.776 ICTA 1988 does not say in terms that only the gain attributable to the part so acquired or developed is taxable but it would seem to follow that this should be the case from the just and reasonable approach to the computation of the gain in s.776(6) ICTA 1988. There may be circumstances where this may not be the case.

"Property Deriving its Value from Land"

This includes:

(a) any shareholding in a company or any partnership interest or any interest in settled property deriving its value directly or indirectly from land; and

(b) any option, consent or embargo affecting the disposition of land.

This is a wide definition. It would clearly catch the sale of a majority holding of shares in a property owning company when a "break up" or assets valuation would be appropriate. A minority holding in a land owning company might not be valued on an assets basis but rather on an earnings basis. S.776(4) ICTA 1988 can also require control to pass and a minority shareholding would not pass this.

S.777(5) ICTA 1988 provides that in determining whether the value of any right is derived from other property, value may be traced through any number of companies, partnership and trusts. Property held by any company, partnership or trust is to be attributed to the shareholders, partners or beneficiaries at each stage "in such manner as is appropriate in the circumstances". It is also to apply for valuation purposes. This is also a very wide provision giving scope for many different views in respect of any given set of facts. In broad terms, the effect is that "value" may be traced through any number of companies on a just and reasonable basis.

"Capital Amount"

By s.777(13) ICTA 1988 this means "any amount, in money or money's worth, which apart from the principal section, [i.e., s.776] does not fall to be included in any computation of income for purposes of the Tax Acts and other expressions including the word "capital" shall be construed accordingly".

The phrase in the operative provisions in s.776 is "gain of a capital nature". This is not defined as such. However, by s.777(13) the word "capital" included in other expressions is to be construed in accordance with the definition of capital amount in that section.

In *Page v Lowther* (see Appendix I) Slade LJ considered that to describe the premiums other than as gains of a capital nature would "fly in the face of reality and the ordinary use of language" (see also *Chilcott v IRC* [1982] STC 1 (see Appendix I)).

S.776 does not apply where Schedule D Case I applies - it does not need to in order to fulfil its purpose.

"In the absence of evidence to the contrary from the taxpayer these gains must be assumed ... to be of a capital nature" (Vinelott J in *Sugarwhite v Budd* [1987] STC 491 at 501). Thus the onus is on the taxpayer to show that it is not a gain of a capital nature. Proving a negative can be difficult.

Disposal of Land

A disposal is a necessary condition for the application of s.776 ICTA 1988. However, the disposer is not necessarily the person who is chargeable.

"Disposal" is not defined as such but is to include direct and indirect disposals. As one learned commentator has suggested, whilst one might think at the start that everyone knows what disposal means, as one reads the relevant subsection the doubts creep in. S.776(4) provides that for s.776 "land" is disposed of if, by any one or more transactions, or by any arrangement or scheme, whether concerning the land or property deriving its value from the land, the *land, or control over the land*, is effectually disposed of. This is extended by s.777(2) ICTA 1988 which provides that account should be taken of any method, however indirect, by which:

(a) any property or right is transferred or transmitted; or

(b) any value of property or right is enhanced or diminished,

and accordingly the occasion of a transfer or transmission of any property or right, however indirect, and the occasion when the value of the property or right is enhanced, may be an occasion when, under the principal sections, tax becomes chargeable.

Subsection (3) of s.777 ICTA 1988 further extends this by providing that this applies in particular to:

(a) sales, contracts and other transactions made otherwise than for full consideration or for more than full consideration; and

(b) any method by which any property or right or the control of any property or right is transferred or transmitted by assigning share capital or other rights in the company or any partnership or interest in settled property; and

(c) the creation of any option or consent or embargo affecting the disposition of any property, and consideration given for the option, or for the giving of the consent or the release of the embargo; and

(d) the disposal of any right or rights on the winding-up, dissolution or termination of any company, partnership or trust.

A direct disposal for these purposes would include a sale of land bought as an investment which the owner has decided to develop for profit before the sale.

Indirect disposals are also included.

Any number of transactions may be regarded as constituting a single arrangement if a common purpose can be discerned in them or if there is other sufficient evidence of a common purpose. The common purpose does not need to be tax avoidance (s.776(5)(b) ICTA 1988 and *Page v Lowther* [1983] STC at 801).

In broad terms the transfer of effective ownership and enjoyment is sufficient to be a disposal for s.776 purposes.

Charge under S.776

Persons Assessable

The gain of a capital nature must have been obtained by a person acquiring, holding or developing the land or by any connected person within the s.839 ICTA 1988 definition (or where any arrangement or scheme is effected as respects the land which enables a gain to be realised by any indirect method or by a series of transactions, by the person who is a party to or concerned in the arrangements or the scheme). Liability can also arise and a person may be taxed, where directly or indirectly (including by premature sale or otherwise) he transmits the opportunity of making a gain to another person. The recipient's gain may then be taxed on the provider of the gain (see subss.(5) and (8)).

For these purposes any number of transactions may be regarded as constituting a single arrangement or scheme if a common purpose can be discerned in them or if there is other sufficient evidence and common purpose. This is exceptionally wide (see s.776(5)(b)).

One does not need the legal ownership to transfer the opportunity to make the gain (see *Yuill v Wilson* (1980) 52 TC 674).

A person deriving value may be charged (see *Yuill v Wilson* supra).

On recovery of tax for a person who realised the gain by the person assessed where an assessment arises under s.776, see s.777.

The persons chargeable are thus the owner of the land and persons connected with him and persons concerned in a scheme or arrangement to realise a gain by an indirect method.

Computation of the Gain

The gain is assessed on a current year basis.

By s.776(6) "such method of computing a gain shall be adopted as is just and reasonable in the circumstances". This is to be done taking into account the value of what is obtained for the disposal of the land and allowing any such expenses as are attributable to the land disposed of. This does not appear to be either the straight trading computation or the CGT computation. It is further provided in subs.(6)(a) that where a freehold is acquired and a reversion is retained on disposal, account may be taken of the way in which the profits or gains under Case I of Schedule D of a person dealing in land are computed in such a case. Thus a premium could be treated as a trading receipt (see *Hughes v B.G. Utting & Co* [1940] AC 463). S.99 ICTA 1988 which provides that s.34 ICTA 1988 is to have precedence over trading receipts is also to apply for s.776 purposes (see s.776(6)(b) ICTA 1988).

By s.777(6) ICTA 1988 any expenditure or receipt or consideration, etc., is to be apportioned by such method as is just and reasonable in the circumstances.

Non-Residents

The section is not limited to UK residents. By s.776(14) ICTA 1988 it applies to all persons whether resident in the UK or not. Further, where it appears to the Board of Inland Revenue that a person entitled to consideration is not resident in the UK the Board may direct that withholding of basic rate income tax (under the s.349(1) ICTA 1988 procedure) shall apply to payments taxable under s.776 (s.777(9) ICTA 1988). This presumes that the Revenue will know of the payment before it is made. In most cases this is unlikely to be the case. If a direction is made payment will have to be made subject to deduction of basic rate income tax which the payer must remit to the Inland Revenue.

The Clearance Procedure

S.776(11) ICTA 1988 provides a clearance mechanism for matters falling in paragraphs (a) and (c) of s.776(2). These are:

i acquisition of land or property deriving its value from land with the sole or main object of realising a gain from disposing of the land; and

ii development of land with the sole or main object of realising a gain from disposing of the land when developed.

There is no clearance procedure for para (b) of s.776(2) ICTA 1988 relating to land held as trading stock.

Application is to be made to the local Inspector of Taxes. Application can be made by a person who considers subs.(2)(a) or (c) may apply to him. The section applies both where a gain has been obtained and where a gain may be obtained under a proposed disposal. In other words, clearance may be given both prospectively and retrospectively.

The applicant must supply written particulars as to how the gain has arisen or may arise. The particulars must make full and accurate disclosure of all material facts and considerations.

The Inspector is to notify his decision within 30 days of receipt of the particulars. There is no power to obtain further information and start time running again, so if in doubt the Inspector may well have to refuse the application.

The section applies to non-residents as well as UK residents. A non-resident may not have an "inspector to whom he makes returns." Technically such a person may not be able to seek clearance. It is understood that the Inland Revenue can be helpful in such circumstances even if only on an informal basis.

It seems in practice that in many cases application is not made.

Exceptions

There are some specific exemptions from the charge under the section. In addition, no charge under the section will arise when the transactions are trading and so fall within Schedule D Case I.

There is an exception for capital gains on principal private residences which would fall within the relief in ss.101-105 CGTA. There is no principal private residence relief for CGT if the residence was acquired with a view to making a gain (s.103(3) CGTA). For these purposes principal private residence relief is treated as being available notwithstanding s.103(3) CGTA.

S.776(10) ICTA 1988 provides that:

> "Where there is a disposal of shares in - (a) a company which holds land as trading stock; or (b) a company which owns directly or indirectly 90% or more of the ordinary share capital of another company which holds land as trading stock, and all the land so held is disposed of in the normal course of its trade by the company which held it, and so as to procure that all opportunity of profit in respect of the land arises to that company, then this section [i.e., s.776] shall not by virtue of subs.(2)(i) [connected person, etc] apply to any gain to the holder of shares as being a gain on property deriving its value from that land (but without prejudice to any liability under para (ii) of the said subs.(2))."

For a discussion and example of this, see *Chilcott v IRC* (see Appendix I).

Revenue Power to Obtain Information (s.778)

The Revenue are given wide powers to obtain information for s.776 ICTA 1988 purposes by s.778 ICTA 1988. There is a special exemption for solicitors but not for accountants (see *Essex v IRC* (1980) 53 TC 720).

Relationship with Capital Gains Taxation

The inter-relationship of s.776 ICTA 1988 with CGT can be an important matter. If consideration is chargeable to income tax, the income tax charge takes precedence over CGT (see s.31(1) CGTA). If a later CGT charge arises it is understood that in practice the amount charged to income tax forms the acquisition consideration notwithstanding that there is no specific provision to this effect in the legislation.

The Vendor and s.776 ICTA 1988

Introductory Comments

It is the Vendor that is most likely to be affected by the section as the Vendor is the most likely person in the development to make a gain of a capital nature rather than a trading profit. The Developer is likely to be a trader or will not make a disposal for some considerable time if at all.

The Financier may well be exempt from direct taxes. However, s.505 ICTA 1988 may not exempt a charity. This section does not contain an exemption for Schedule D Case VI purposes. Great care is needed in such circumstances.

The purpose of this section is to consider the effect of certain common transactions which a Vendor might undertake and the impact (if any) of s.776 ICTA 1988.

These are:

(a) applying for planning permission;

(b) putting in some of the infrastructure (e.g., sewers and/or spur roads);

(c) purchasing in extra land;

(d) profit-sharing agreement;

(e) price plus profit share.

Application for Planning Permission

This of itself should have no effect. It is a commercially sensible approach to maximising the realisation of an investment. It should not of itself give rise to a trade or an appropriation to trading stock (see *Taylor v Good* supra). It would not fall within subs.(2). Consequently it should have no effect for the purposes of the section.

Putting Infrastructure In

This might get close to trading and in some circumstances could cross the line with an appropriation to trading stock. This will depend on the precise circumstances.

If what was done could be said to amount to development but was short of a trade then subs.(2)(c) (development with the main object of realising a gain from disposing of the land when developed) might come into play. The amount to which the section could apply would be limited by subs.(7). Under this "subs.(2)(c) of this section shall not apply to so much of any gain as is fairly attributable to the period, if any, before the intention to develop the land was formed..." This may allow much scope for argument depending on the precise circumstances.

A great deal would need to be done before there was any VAT saving.

Purchase in of Land

If extra land is bought in to sell on, this is very likely to amount to trading. *Pilkington v Randall* supra is authority for this.

The land already owned would seem to be appropriated to trading stock. If this is the case there would seem to be scope for the section to apply. If trading is not involved then the section could apply and careful analysis of all the circumstances will be necessary.

Profit-Sharing Agreement

The landowners might agree to share the land profit by equalising the price.

This would seem likely to give rise to a partnership and/or an appropriation to trading stock and a trading charge. If there is no trade then subs.(2)(c) might come into play.

Sale for Price Plus Development Profit Share

Great care would need to be taken here. In effect this was what the trustees did in *Page v Lowther* supra.

In that case they shared in part of the development profit. If, instead, the price for the sale of the land could be £x per acre plus a percentage of the value of the land on the obtaining of planning permission, this would arguably (at least) not be sharing in the development proceeds.

APPENDIX I

Summary of Cases under s.776

Yuill v Wilson [1980] STC 460, [1980] 3 All ER 7 (HL)

The taxpayer was a director and the chairman of Y Ltd, in which he and his family held the controlling interest. P Ltd, of which the taxpayer and family trusts were the shareholders, was formed in 1961 and a parcel of land (the Fen land) was conveyed to P Ltd by Y Ltd for £4,050. In 1966 Y Ltd agreed to buy 108 acres of land known as Quarry Farm for £194,400, the purchase to be completed in stages after 1972. D Ltd, of which the taxpayer and another director of Y Ltd were the directors, was formed in 1972 and on the direction of Y Ltd 27 acres of the Quarry Farm land were purchased for £48,000 and conveyed to D Ltd. Settlements with non-resident trustees were formed in September 1972 who themselves formed or acquired two Guernsey companies, C Ltd and M Ltd. In December the same year P Ltd sold at full market value a substantial proportion of the Fen land to C Ltd, which resold it in 1974 to Y Ltd for £700,000. In 1973 D Ltd had sold to M Ltd the land conveyed to it for £81,000 (also full market value). Later in 1973, M Ltd acquired a further 54 acres of the Quarry Farm land from D Ltd. M Ltd later sold the Quarry Farm land to Y Ltd for £648,000. Consequently, three-quarters of the Quarry Farm land which Y Ltd had agreed to buy for £194,400 became Y Ltd's again for £648,000 and the Fen land became its property for £700,000. The majority of the purchase price for both transactions was, however, deposited with a third party, to be dealt with in certain ways depending on events. The taxpayer was assessed on the gains made under [s.776]. The Commissioners found that there was a scheme or arrangement or a series of transactions which enabled capital gains to be made by C Ltd and M Ltd on the sale of land to Y Ltd and, further, that the taxpayer either directly or through his companies and with the help of his Guernsey trustees obtained for C Ltd and M Ltd the gains which fell within [s.776]. The taxpayer appealed. It was held that the disposal of the land at full market value to C Ltd and M Ltd did not preclude the application of [s.776], since [s.776] applied to any gain which fell within the language of the section and contained an element of tax avoidance. Further, the Commissioners' finding that the taxpayer had obtained the gains for the Guernsey companies with the help of his trustees necessarily implied that he `indirectly' provided those companies with an opportunity of realising those gains in such a way as to attract the application of [s.776(8)]. However, for a capital gain realised by another person to be taxable as a capital gain realised by the taxpayer under [s.776(8)] the gain had to be enjoyed or disposed of by that other person. Since the majority of the purchase price for both transactions had been deposited with a third party, neither C Ltd nor M Ltd could enjoy or dispose of those sums. The taxpayer was therefore only chargeable under Schedule D Case VI on a gain of £1,417 made by M Ltd.

Yuill v Fletcher [1984] STC 401

Further litigation took place on the same facts as in *Yuill v Wilson* but for a different year based on the House of Lords indication that tax would be assessable on the release of the deposits.

Page v Lowther [1983] STC 799 (CA)

The trustees of a settled estate granted a lease of 2.6 acres of land included in the estate to a development company, TH Ltd, for a period of 99 years in return for a rent and a premium. The premium was to be payable not on the grant of the lease but as a predetermined proportion of the price of underleases granted by TH Ltd of the properties to be built on the land. [S.776] clearance was sought and refused in November 1970. Development began in 1971 and between 1973 and 1976 the trustees received premiums totalling £1.5m. They were assessed to income tax on the ground that the transaction fell within [s.776(2)(c)]. On appeal, the Commissioners found that the development had been carried out solely by TH Ltd and that the trustees were not `connected' with TH Ltd within the meaning of para (c)(ii); the trustees had disposed of the land before development had begun and the provisions in the head lease for payments related merely to the calculation of the premiums payable to the trustees on the grant of underleases by TH Ltd; the premiums did not constitute gains of a capital nature obtained from the disposal of land when developed; the lease and the underleases did not constitute an `arrangement or scheme' and so the trustees were not liable to tax under Schedule D Case VI. The Crown appealed on the grounds that the only premiums payable were those payable on the grant of an underlease and that accordingly a gain of a capital nature was obtained by the trustees from the disposal of land when developed and that the lease constituted an `arrangement' which enabled a gain to be realised by the trustees from a series of transactions. Warner J at first instance allowed the Crown's appeal. The trustees appealed. It was held that the wording of [s.776(1)] was not sufficiently clear to limit the operation of the section to transactions specifically designed to avoid tax and the sidenote to s.488 TA 1970 (Artificial Transactions in Land) could not be relied on as a guide to construction. Under [s.776(5)] any number of transactions were capable of being regarded as constituting a single arrangement or scheme if a common purpose could be discerned in them and, for the purposes of [s.776(2)], it was sufficient if that common purpose were to enable a gain to be realised by a party to the arrangement. "On any footing and on any possible construction, it, i.e., the word "arrangement" must be wide enough to include the lease of 1971." (per Slade LJ [1983] STC 799 at 806a). The execution of each underlease was the first occasion when the trustees became entitled to payment as against the underlessees (who were actually going to pay the premium) and "in these circumstances, to hold that they, i.e., the trustees had received no gain of a capital nature from the disposals effected by the underleases would ... be to fly in the face of reality and the ordinary use of language." (per Slade LJ at 806g). The trustees were therefore parties to an arrangement as respects land which enabled them to realise a gain by an indirect method or series of transactions and they were accordingly liable to tax under [s.776].

Chilcott v IRC [1982] STC 1 (ChD)

The taxpayers were the directors and shareholders of K Ltd. In 1969 K acquired a warehouse at its then market value of £30,000 and, three years later, it agreed to sell the warehouse to M Ltd for £1.9m, to be satisfied by the allotment of shares in M Ltd, subject to renounceable letters of allotment. On the same day the taxpayers agreed to sell the issued share capital of K Ltd to THH (which was not connected with K Ltd

or M Ltd) for £1,233,235, to be satisfied by cash or fully paid shares in M Ltd or by shares in any other agreed company. Completion of the shares agreement was to take place within seven days of completion of the land agreement. The land agreement was completed and, on the same day, the transfer of the shares in K Ltd to THI Ltd (THH's parent) was approved, the taxpayers having resigned as directors of K Ltd and nominees of THH having been appointed in their place. THH later procured the renunciation in favour of the taxpayers by K Ltd of a number of the M Ltd shares which K Ltd had received on completion of the land agreement, in satisfaction of the purchase price of the shares in K Ltd. The taxpayers were assessed to tax, the Crown taking the view that the transactions fell within [s.776(2)(i)] because the sums received in the form of M Ltd shares for the sale of their K Ltd shares represented gains of a capital nature obtained by the disposal of land and the transactions constituted an arrangement or scheme `as respects the land'. The taxpayers appealed, contending that the land was trading stock of K Ltd and that K Ltd did not make a gain of a capital nature and there was no arrangement or scheme in respect of the land for the purposes of subs.(2)(ii). The Special Commissioners dismissed the appeal. The taxpayers appealed again. It was held that [s.776(2)(i)] was not intended to apply where a gain of a capital nature was obtained by the sale of shares in a company unless by virtue of subs.(4) the disposal could be treated as a disposal of land. Also, the exemption in [s.776(10)] applied as the disposal was of shares in a company which held land as trading stock. It was further held that the transactions were not an arrangement or scheme within [s.776(2)(ii)] (consequently the transactions were not within [s.776]).

Winterton v Edwards [1980] STC 206, [1980] 2 All ER 56 (ChD)

L was a property developer who operated through a group of some seventy companies. The taxpayers, W and B, were employees of the principal company and owned 4.5% and 5% respectively of the shares of the principal company. L owned the remaining 90.5%. W and B also subscribed for 5% each of C Ltd, which developed a site and used the Bradman scheme to reduce liability to betterment levies. This scheme was later used in a number of transactions within the group. In 1970 W and B discovered that L had embarked on two property development schemes on his own account but using the facilities of the group to enhance the values of the properties concerned. When they protested, L agreed to give W and B a 4.5% and a 5% share in the two ventures, which shares were stated to be held in trust by L for W and B absolutely. In 1970-71, both received £20,000 and in 1971-72 W received £21,395 in total and B, £24,495, as well as the release of a debt of £1,500. The taxpayers were assessed to tax under [s.776] and were held liable to tax in the year 1970-71 on the whole of the gains they had received in 1970-71 and 1971-72. The taxpayers were found to be `concerned in' the schemes within [s.776(2)(ii)] because (a) on the facts it was clear that L had acquired the land with the sole or main purpose of realising a gain from disposing of it and it had been developed with that object in view, (b) tax-avoidance schemes had been set up, (c) the taxpayers were `concerned in' the schemes because of their 4.5% and 5% shares in the proceeds and (d) the schemes `enabled a gain to be realised' by the taxpayers within s.776(2)(ii). Although most of the benefit was actually received in 1971-72, it nevertheless fell to be assessed for 1970-71 as there was nothing to prevent the taxpayers from disposing of their rights under the trust for a share in the proceeds in 1970-71.

Sugarwhite v Budd [1987] STC 491 ChD

In 1973 the taxpayer purchased a property for £20,000. Later in the same year, the taxpayer, through arrangements made by K, contracted to sell the property to M Ltd,

a company with an address in the Bahamas. M Ltd was entitled under the contract to nominate another purchaser and the property was transferred on completion to T Ltd for £33,500, the taxpayer receiving £25,000, M Ltd £1,000. The balance was divided between two companies with addresses in the Bahamas, C Ltd (£6,500) and G Ltd (£1,000). The taxpayer was assessed to tax under [s.776] on the gains accruing to the Bahamian companies. The Special Commissioner found that the taxpayer was a party to the arrangement under which the property was sold to T Ltd and his share of the gross profits was fixed at £5,000, the balance being divided with his consent amongst the Bahamian companies. In the absence of evidence to the contrary from the taxpayer, the gains transmitted to the Bahamian companies must be assumed to be of a capital nature and the transaction was therefore within [s.776]. The taxpayer, although it was not disputed that to the extent that a gain of a capital nature was made by the Bahamian companies the transaction fell within [s.776], appealed on the ground that the Bahamian companies were parties to a joint trading adventure and that the sums paid to them were income chargeable to income or corporation tax rather than under [s.776]. However, since:

> "all that is known of this transaction is that at the time when the taxpayer was looking for a purchaser he entered into a contract for sale to M Ltd at an under-value and that when a purchaser had been found the difference between the price on the sale to M Ltd and the price paid by the arm's length purchaser was shared. If the taxpayer had wished to claim that the Bahamian companies engaged in trading transactions or in transactions under which monies were received by them other than as capital it was for him to put before the commissioner evidence as to precisely what happened." (per Vinelott J, [1987] STC 491 at 500j).

In the absence of such evidence the gains must be assumed in all the circumstances to be of a capital nature.

The Court of Appeal dismissed the taxpayer's appeal ([1988] STC 333).

APPENDIX II

Outline of Points to Consider on s.776

(1) Is land or property deriving its value from land involved?

(2) Has there been development or is development in contemplation?

(3) (a) Has the land (or property deriving its value from land, e.g., shares) been acquired with the sole or main object of realising a gain on the disposal? or

(b) Is the land held as trading stock? or

(c) Has the land been developed with the sole or main object of realising a gain when developed?

(4) Has a gain of a capital nature been obtained?

(5) Was that gain obtained

(a) by the person acquiring, holding or developing the land or any connected person? or

(b) by any person who is a party to or connected in a scheme or arrangement to enable the gain to be realised by any indirect method or any series of transactions?

(6) What was the main object of the transaction? Was it realising a gain from the land, property deriving its value from the land or control of such assets?

(7) Was a gain made which does not fall within the computation of liability to UK taxation on income?

(8) Has the owner or any other person made a capital gain?

(9) Was the other person:

(a) connected with the owner?

(b) party to or concerned in a series of transactions or an indirect method of realising a gain?

(10) Is there any property deriving its value from land?

(11) Does anyone have control over such property or the land?

If the answers to 3 - 5 are yes, then s.776 ICTA 1988 *prima facie* applies which allows the gains to be treated as of an income nature taxable under Schedule D Case VI.

Notes:

(1) There is a clearance procedure under s.776(11) ICTA 1988 for matters falling within s.776(2)(a) and (c) ((a) acquisition and (c) development with main object of realising a gain) not for s.776(2)(b) (land held as trading stock).

(2) There are wide extensions to s.776 in s.777 ICTA 1988

(3) There is a wide extension to providing opportunities to make a gain in s.776(8).