

Business asset disposal relief anti-forestalling

(Lecture P1240 – 24.40 minutes)

The cumulative lifetime limit for the relief which has been renamed business asset disposal relief was reduced from £10,000,000 to £1,000,000 for transactions taking place on or after 11 March 2020 (Paras 1 and 2 Sch 3 FA 2020).

The FA 2020 legislation contains a number of anti-forestalling rules to counter arrangements which sought to lock in entitlement to the higher level in anticipation of the abolition or restriction of the relief. Planning of this sort typically required the making of an election under S169Q TCGA 1992 and is addressed by Paras 4 and 5 Sch 3 FA 2020.

S169Q TCGA 1992 allows an election to be made which displaces the operation of S127 TCGA 1992, i.e. that a share reorganisation is not regarded as a disposal of the original shares. Reorganisations include share-for-share exchanges and company reconstructions. This chapter considers the position with regards to share-for-share exchanges.

The aim of the election is to allow a disposal to be triggered upfront, so as to create a gain against which relief can be set, given that business asset disposal relief may not be available on the sale of the new shares.

If a S169Q TCGA 1992 election is made on or after 11 March 2020 in relation to a share-for-share exchange under S135 TCGA 1992 which took place between 6 April 2019 and 10 March 2020 (inclusive), relief will still be available but subject to the reduced limit of £1,000,000. The detailed provisions for this anti-forestalling rule are found in Para 5 Sch 3 FA 2020.

The rule applies where there is an exchange of shares or securities within the meaning of S135 TCGA 1992 and either of two conditions are met (note the references to 'company A' and 'company B'):

1. those holding shares or securities in company B immediately after the exchange are substantially the same as those who held shares or securities in company A; or
2. those having control of company B immediately after the exchange are substantially the same as those who had control of company A.

Various permutations are examined in the examples which follow. Unless otherwise specified, they all involve trading companies.

Example 1

Chris and Dick each hold 50% of the shares in company A. Prior to 11 March 2020, they incorporate company B which issues them with new shares in exchange for their shares in company A. This is regarded as a share reorganisation and so Chris and Dick are not treated as disposing of their shares in company A.

Following the reduction in the lifetime limit, Chris and Dick could elect under S169Q TCGA 1992 to crystallise a gain which would theoretically qualify for relief under the £10,000,000 limit, even though they would still be eligible for business asset disposal relief (subject to the new limit) when they sell their shares in company B.

The two parties (Chris and Dick) are exactly the same individuals and so the condition set out in 2. above is met. The reduced limit is therefore in point.

Example 2

Richard and Sheila are a married couple. They each own 50% of company A. Together with their two adult children, Timothy and Rupert, they set up company B and exchange their shares in company A for an issue of shares in company B, with the parents having an 80% stake and the sons a 20% stake. Assume that they use the same time frame as Chris and Dick.

Because FA 2020 treats connected persons (as defined in S286 TCGA 1992) as the same person for this purpose, the shareholders in each company are treated as being the same and so the condition set out in 1. above is met. Again, the lower limit is in point.

Example 3

Nigel and Cindy are a married couple. They each own 50% of company A. A third party wishes to invest in the business via company B. Nigel and Cindy exchange their company A shares for an issue of shares in company B so that together the couple hold a 60% stake in company B. Assume that they use the same time frame as Chris and Dick.

Taking into account the extent of the third party's holding the shareholders would not in this instance be considered to be substantially the same. The anti-forestalling legislation dealing with the holding of shares should not apply. HMRC are a little less specific, as is evidenced by their statement:

‘Whether the shareholders would be regarded as being substantially the same will depend on the facts. Where, say, there are two original shareholders in company A but a third in company B who is not connected and holds a substantial (but not majority) proportion of the shares in that company, then the rule *may* (emphasis added) not apply.’

But see below.

The second condition above deals with the situation where the parties involved do not hold shares in the respective companies but are classified as ‘associates’ under the close company legislation.

Example 4

Owen owns 100% of company A. The XYZ trust was settled by Owen's late father and the trust beneficiaries comprise Owen's children and grandchildren. The XYZ trust holds all the shares in company B, a long-established family investment company.

In December 2019, Owen exchanged his company A shares in return for:

- cash of £1,500,000; and
- an issue of shares in company B.

The shares in companies A and B are not held by persons who are connected with each other under S286(3) TCGA 1992 – see Para CG14590 of the Capital Gains Manual. However, Owen and the trustees of the XYZ trust are associates by virtue of S448 CTA 2010, given that the settlor of the trust was a relative of his. Companies A and B are therefore treated as being under the same control.

Owen will be taxed on the cash element at the time of the share-for-share exchange and will be able to claim relief based on the 'old' limit of £10,000,000. If Owen makes a S169Q TCGA 1992 election, the gain attributable to the consideration which he received in the form of shares in company B will attract relief at the reduced level of £1,000,000 (less any relief which he previously enjoyed).

The rule explained in Example 4 could also apply to the situation described Example 3 because Nigel and Cindy are associates who together control company B through their 60% shareholding. However, it would not apply if the outside third party's shareholding meant that Nigel and Cindy did not control company B.

Finally, there is an additional provision which applies where a share-for-share exchange takes place on the departure of a shareholder. If the remaining shareholders have a greater shareholding in company B than they did in company A, they are subject to the reduced limit where they still meet the qualifying conditions for relief in respect of their shares in company B on 11 March 2020 (Para 5(3) Sch 3 FA 2020).

Example 5

Donald, Edward and Francis have had equal shareholdings in company A for several years, but Donald wishes to retire from the business. Edward and Francis therefore set up company B and, in October 2019, they exchanged their shares in company A for an issue of shares in company B. Contrast their position with that of Donald who received cash and loan notes in company B (but no shares).

Donald would not meet the relief conditions in respect of company B on 11 March 2020 because the company is not his personal company and he is no longer an officer or employee. Therefore, Donald can make an election under S169Q TCGA 1992 and the 'old' limit of £10,000,000 will be available. If Edward or Francis make a similar election, their gain will be subject to the £1,000,000 limit.

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