

## Sale of a company following a hive-down (Lecture B1384 – 26.18 minutes)

### *Introduction*

In a previous session, we looked at the tax implications of hiving a trade and its assets to a new company owned by the existing group. This usually precedes a sale of the new company to a third party.

This session considers the tax implications of the sale on the vendor and the purchasing company.

### *Potential chargeable gain on disposal of Newco*

There are two issues to consider:

1. Whether the vendor company qualifies for SSE on disposal of shares in Newco;
2. If not, then possible de-grouping gains if Newco received chargeable assets or intangible assets at NG/NL on the hive down.

### *De-grouping charges (s.179 TCGA 1992)*

Where chargeable assets have been previously transferred within a 75% gains group at NG/NL and the recipient company leaves the 75% group within 6 years of receiving the asset, a gain arises, calculated as the market value of the asset when it was received minus the indexed cost to transferor company.

This is generally taxed on the company leaving the group, but the gain can be transferred to another 75% group company using a s.171A election.

Where the de-grouping gain arises as a result of a disposal eligible for substantial shareholding exemption (SSE – see later), the de-grouping gain is treated as part of the consideration for the sale of the shares (S.179(3D)), and is also exempted.

### *De-grouping charges and intangibles (s782A CTA 2009)*

A similar treatment to the above applies to de-grouping charges involving intangible assets where the share sale is eligible for SSE, but there is one difference.

Instead of calculating a profit or loss by reference to the market value of the intangible when it was transferred to the receiving company and then exempting it, the intangible retains its tax written value going forward (it is not rebased to current market value).

### *Example*

A Ltd is the parent company of a trading group. In May 2023, the long-held trade of a subsidiary, C Ltd is hived down to Newco Ltd including:

- Land and buildings: market value £500,000, indexed cost to Dec 17 £310,000
- Intangible asset: market value £200,000, tax WDV £120,000

In June 2023, the shares in Newco Ltd are sold to a third party for £2.1 million. Amortisation on the intangible of £8,000 was charged for June 2023.

Assuming the share sale qualifies for SSE, what are the tax implications relating to the land and buildings and intangible asset?

#### *Analysis*

A de-grouping gain arises on the land and buildings of (500 – 310) £190,000. This is added to the share consideration of the sale of Newco and so is exempted by SSE.

The base cost of the land and buildings in Newco is £500,000 going forward (as it is deemed to dispose and reacquire them for this amount).

The intangible asset does not give rise to a de-grouping charge where SSE applies to the share sale.

The base cost of the intangible asset is £120,000 (i.e. the tax WDV when transferred to Newco).

Amortisation of the intangible will be deducted in the CT600 but based on the tax WDV when acquired (£120,000) not the market value at that date (£200,000).

If Newco is amortising £200,000 in its accounts, this will lead to a partial disallowance in the CT computation.

#### *SSE conditions*

Broadly, the vendor must have held 10% or more of a trading company for a period of 12 months in the previous 6 years.

The 10% means 10% of ordinary share capital, entitlement to 10% of profits available for distribution, and entitlement to 10% of assets available to equity holders in a winding up.

There is no minimum percentage holding to qualify if the shares are worth more than £50m.

Whilst the company being sold must be a trading company, the vendor does not need to be.

If a trade is hived down to a new company then sold shortly afterwards, the 12 month test will not be satisfied, but Para 15A, Schedule 7AC TCGA 1992 allows the inclusion of periods where another group company carried on the trade transferred to Newco

#### *Para 15A, Sch 7AC TCGA 1992*

(2)...the period for which the investing company is treated as holding a substantial shareholding in the company invested in is extended in accordance with sub-paragraph (3) if the following conditions are met.

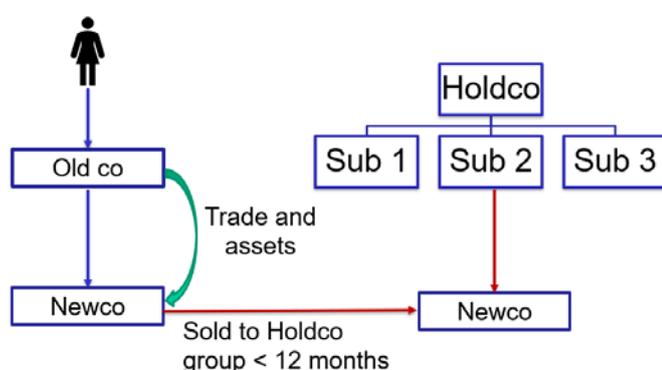
- a) immediately before the disposal, the investing company holds a substantial shareholding in the company invested in,
- b) an asset which, at the time of the disposal, is being used for the purposes of a trade carried on by the company invested in was transferred to it by the investing company or another company,

- c) at the time of the transfer of the asset, the company invested in, the investing company and, if different, the company which transferred the asset were all members of the same group, and
- d) that the asset was previously used by a member of the group (other than the company invested in) for the purposes of a trade carried on by that member at a time when it was such a member.

2A) ...irrelevant (to do with oil and gas businesses)

- (3) The investing company is to be treated as having held the substantial shareholding at any time during the final 12 month period when the asset was used as mentioned in subparagraph (2)(d) (if it did not hold a substantial shareholding at that time)

*But what if there was no group before the hive down?*



### Analysis

There was no group in place when Old co was running the trade so S2(d) Para 15A, Sch 7AC TCGA not satisfied. No SSE is available on disposal of Newco

Degrouping gains will arise on chargeable assets and intangible assets transferred to Newco.

If a dormant company was owned by Old co prior to the hive down, s2(d) would have been satisfied and SSE would have been available. The trade would have been run by a member of the Old co group (i.e. it plus the dormant company constitutes a group). This seems strange, but with no dormant company, SSE is not available.

### Other conditions to use Sch 7AC.15A

S19(1): The newco must be a trading company immediately after the sale of the shares

S19(2B): The company invested in is treated as having been a trading company at any time during the final 12-month period when the asset was used as mentioned in paragraph 15A(2)(d) (by another group member)

A newco (or previously dormant company) needs to trade for at least a day to meet s15A 2(b) (to 'use the asset in a trade').

### *Preservation of trading losses when company changes ownership*

“Major change in nature or conduct of trade” (MCINOCOT) provisions (s673 CTA 2010) operate to restrict losses carried forward where there is a change in ownership of a company. This is a much more sensitive test than the usual (pre-1 April 2017 loss) carry forward rules.

- If a MCINOCOT occurs in the 8 year-period from 3 years before the change in ownership to 5 years after, losses cannot be carried forward beyond the date of change in ownership.
- If the MCINOCOT occurs before the change in ownership, no losses can be carried forward for the new owner to use.
- If the MCINOCOT occurs in the 5 years after change of ownership, losses carried forward at the change of ownership are cancelled retrospectively.

Post 1 April 2017 pre-acquisition losses brought forward of an acquired company cannot be group relieved to the new group members for 5 years.

### *What is a MCINOCOT?*

Major change in

- a) Type of property dealt in; or
- b) Services or facilities provided; or
- c) Customers, outlets or markets; or
- d) If the level of business has become negligible and revived.

### *HMRC examples – no MCINOCOT*

- A company manufacturing kitchen fittings, in three obsolescent factories moves production to one new factory (increasing efficiency)
- A company manufacturing kitchen utensils replaces enamel with plastic, or a company manufacturing time pieces replaces mechanical by electronic components (keeping pace with developing technology)
- A company operating a dealership in one make of car switches to operating a dealership in another make of car satisfying the same market (not a major change in the type of property dealt in)
- A company manufacturing both filament and fluorescent lamps (of which filament lamps form the greater part of the output) concentrates solely on filament lamps (a rationalisation of product range without a major change in the type of property dealt in)
- A company whose business consists of making and holding investments in United Kingdom quoted shares and securities makes changes to its portfolio of quoted shares and securities (not a change in the nature of investments held)

*HMRC examples - MCINOCOT*

- A company operating a dealership in saloon cars switches to operating dealership in tractors (a major change in the type of property dealt in)
- A company owning a public house, switches to operating a discotheque in the same, but converted, premises (a major change in the services or facilities provided)
- A company fattening pigs for their owners, switches to buying pigs for fattening and resale (a major change in the nature of the trade, being a change from providing a service to being a primary producer)
- A company switches from investing in quoted shares to investing in real property for rent (a change in the nature of investments held).'

*Contributed by Malcolm Greenbaum*