

Voting rights

(Lecture P1217 – 11.03 minutes)

The issue in the somewhat unusual First Tier Tribunal case of *Holland-Bosworth v HMRC* (2020) was whether the taxpayer (H-B) should be entitled to claim entrepreneurs' relief in respect of a capital gain on a share disposal which took place on 6 December 2014. This sounds like a relatively straightforward exercise, but, as will become clear, the position was not entirely clear-cut.

H-B and another individual (who was not involved in the case) were equal shareholders in The Hayward Holding Group Ltd (Hayward). They held 310 ordinary shares each.

In 2007, H-B sold 273 of his shares to an unconnected company called Towergate. Towergate's shares were subsequently re-designated as 'A' ordinary shares. The 37 Hayward shares H-B retained were re-designated 'B' ordinary shares. This was all done by a special resolution dated 3 August 2007 and signed by Towergate and H-B. The resolution and Hayward's amended Articles of Association were in due course filed with Companies House on 6 February 2010.

H-B remained a director of Hayward after the sale of his shares to Towergate.

On 29 April 2013, H-B acquired a further 13 'B' ordinary shares by way of a bonus issue. This was effected by an ordinary resolution proposed and signed by (amongst others) H-B. The 50 'B' ordinary shares H-B held represented exactly 5% of Hayward's total ordinary share capital. More than one year later, in December 2014, H-B sold his 50 'B' ordinary shares for £1,350,000, realising a gain of £1,294,964, in respect of which entrepreneurs' relief was claimed.

H-B filed his self-assessment tax return for 2014/15 on 26 January 2016, in which he stated that the rights attached to the 'B' ordinary shares were incorrectly described in Hayward's Articles of Association and that, for all intents and purposes, the 'B' ordinary shares had full voting rights.

However, Article 4 of the Articles of Association stated:

'The holders of the 'B' ordinary shares shall not be entitled to receive notice of, attend or vote at any general meeting of the company.'

Article 5 went on to say:

'All or any of the rights for the time being attached to any class of shares for the time being in issue may from time to time (whether or not the company is being wound up) be altered or abrogated with the consent of the holders of not less than three-quarters of the issued shares of that class (the speaker's emphasis) or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of such shares . . . (and) every holder of shares of the class shall be entitled on a poll to one vote for every such share held by him.'

Judge Julian Ghosh outlined his understanding of the company's Articles of Association as follows:

'It is convenient to summarise my conclusion on the construction and application of Article 4 and Article 5 of the Articles of Association at this stage. Article 4 could not be clearer. The holders of the B ordinary shares were not entitled to vote at any general meeting of (the company). Article 5 provides for an "alteration or abrogation" of the B ordinary share rights. An "alteration" or "abrogation" suggests a modification of existing rights . . . Article 5 provides a protection against the modification of share rights which the affected shareholders may not want. Article 5 does not provide for the conferral of share rights, effected by shareholders of a particular class of shares, unilaterally as a class. Article 5 applies to all and any modification of existing rights to shares, nothing more. There is no ambiguity as to the effect of Article 4 and Article 5. These respective Articles simply apply fully on their terms.'

He went on to comment that the 'B' ordinary shareholders could not unilaterally 'arrogate' (i.e. claim without justification) to their shares votes or other rights might have the effect of diluting the rights of other classes of shares by means of an appeal to Article 5.

The relevant voting rights for the purposes of S169S(3)(b) TCGA 1992 have always been understood to be voting rights exercisable in general meeting. The word 'exercisable' means capable of being exercised, whether or not actually exercised (see *Hepworth v Smith* (1981)). Furthermore, in *Boparan v HMRC* (2007), the Special Commissioner decided that votes held by the taxpayer in a parent company did not make the votes held by that company in a wholly owned subsidiary 'exercisable' by the taxpayer.

In other words, the First Tier Tribunal concluded that the company's Articles of Association were sufficiently clear as to leave no doubt as to their construction and Judge Julian Ghosh declined to find as a fact either that Towergate would have consented to an amendment to the Articles of Association (in the absence of any evidence) or that Towergate and H-B considered that the 'B' ordinary shares did have voting rights exercisable in general meeting. H-B's appeal was dismissed.

This case serves as a reminder that it is not sufficient to hold 5% of a company's ordinary share capital in order to satisfy the 'personal company' definition. It is also necessary to comply with the voting rights test and, since 29 October 2018, to meet the further tests relating to beneficial entitlement to profits and assets (or sale proceeds).

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