TAX UPDATE

OCTOBER 2017

INVESTORS' RELIEF
REDUCING CAPITAL GAINS TAX TO 10%

Finance Bill 2016 included new legislation which provides for a new Capital Gain Tax relief for investors in unlisted trading companies. Qualifying gains under the relief are taxed at a reduced Capital Gains Tax rate of 10%, rather than 20% for higher rate taxpayers. The Investor's Relief is subject to a maximum lifetime cap of £10 million of gains.

Qualification requirements

1 - The company that issues the shares must be either a trading company or the holding company of a trading group throughout the share-holding period. 'Trading company' and 'trading group' do not have quite the same meaning as for Entrepreneurs' Relief but the rules are similar;
2 - The relief only applies to holdings of fully paid Ordinary shares in unlisted trading companies;
3 - The shares must be new shares subscribed for by an investor on or after 17 March 2016;
4 - The shares must have been held solely by the shareholder for a period of at least 3 years so in effect only gains arising after 5 April 2019 can qualify;
5 - The shareholder (or anyone connected to them) must not be a remunerated officer or employee of the company at any time during the period of holding the shares.
6 - The shares must have been issued and subscribed for at arm's length for genuine commercial reasons and not as part of a scheme or arrangement the main purpose or one of the main purposes of which was the avoidance tax.

Interaction with Entrepreneurs' Relief

Entrepreneurs' Relief also allows for certain gains by individuals to be taxed at a lower rate of 10% Capital Gains Tax.

As the conditions for Entrepreneurs Relief require an individual to have been an officer or employee of the company during the holding period it is rare that both Investors' and Entrepreneurs' Relief will apply to the same disposal.

Anti-avoidance

Shares which might otherwise qualify for Investors' Relief will be excluded from relief if the investor receives any value from the company, other than receipts of insignificant value, at any time in the period of restriction.

The period of restriction starts one year before the shares are issued and ends on the third anniversary of the issue date.

These provisions mirror closely the 'receipt of value' provisions that apply for other reliefs such as Seed Enterprise Investment Scheme (SEIS) and Enterprise Investment Scheme (EIS).

As with all anti-avoidance provisions, these rules are complex and great care should be taken.

Investors' Relief and reorganisations

It is common under a group reorganisation for an individual to receive shares in a different company to the company originally invested in. Provided the shares are issued on a share for share exchange, the new shares will stand in the shoes of the old shares for the purpose of this relief.

The holding period will include the holding period of both the old and new shares for the purposes of the 3-year requirement.

Conclusion

In our opinion, this is a very useful relief for investors in large unlisted companies that do not qualify for relief under EIS but could also have much wider application.

It is clear that the relief is designed to provide a lower Capital Gains Tax rate for passive investors.

As a consequence of the above the rules for Investors' Relief are more complex than Entrepreneurs' Relief and contain some provisions similar to those found with EIS rules.

The policy is in line with the Chancellors continued promotion of an "enterprise and investment" culture in the UK and may be beneficial to many businesses looking for renewed capital injection or for those individuals who have utilised the maximum amounts of Entrepreneurs Relief already.

Great care will be required to ensure this new relief is available when investing but for the appropriate individual the relief is potentially very valuable.

If you require any further information on any of the issues raised above, please contact your Menzies Relationship Partner.