

## 4

## Anti-Avoidance

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**Cross-references.** See 14.6 COMPANIES for provisions relating to corporate losses; 17 CONNECTED PERSONS; 20 DISCLOSURE OF TAX AVOIDANCE SCHEMES; 21.9 DOUBLE TAX RELIEF for schemes and arrangements designed to increase such relief; 48 OVERSEAS MATTERS for provisions relating to overseas resident settlements; 48.9, 48.10 OVERSEAS MATTERS for interests in controlled foreign companies and in offshore funds respectively; 49.17 PARTNERSHIPS; 61.16 SETTLEMENTS for restrictions on transfer of settlement losses to beneficiary becoming absolutely entitled to settled property; 61.20–61.23 SETTLEMENTS for further anti-avoidance provisions.

## Introduction

[4.1] Anyone attempting to structure a transaction so as to avoid a liability to tax on chargeable gains arising or to mitigate such a liability must consider:

- whether the line of cases often referred to as the ‘Ramsay principle’ will operate to make the arrangements ineffective;
- whether the tax advantage under the arrangements is counteracted by the general anti-abuse rule;
- whether the arrangements give rise to a duty to disclose the details to HMRC under the provisions for DISCLOSURE OF TAX AVOIDANCE SCHEMES (20); and
- whether the arrangements fall foul of one of the many pieces of specific anti-avoidance legislation.

This chapter covers three of these considerations. For (c) above see 20 DISCLOSURE OF TAX AVOIDANCE SCHEMES.

The approach of the courts to avoidance cases is dealt with at 4.2 below, and the rules for the disclosure of tax avoidance schemes are at 20.2–20.5 below. The general anti-abuse rule is described at 4.3 and 4.4 below. The next part of the chapter describes specific anti-avoidance provisions, many of which, it should be noted, apply where the particular conditions are satisfied whether or not there is any intention to avoid tax. Note that there are many anti-avoidance provisions which are dealt with outside this chapter where they relate to legislation described elsewhere in this work. See the list of provisions at 4.5 below and the cross references at the head of the chapter.

FA 2014 has introduced powers that enable HMRC, by way of a ‘follower notice’ to require a person using an avoidance scheme which is defeated in the courts in relation to another taxpayer to concede their position to reflect the court’s decision. See 4.30 onwards below. Powers to enable HMRC to issue an ‘accelerated payment notice’ which requires a user of an avoidance scheme to pay tax upfront before the success or failure of the scheme has been finally determined have also been introduced. See 4.34 onwards below.

### Repayment claims in avoidance cases

HMRC have published their policy on withholding repayment claims in avoidance cases where they are challenging or considering challenging the claim by enquiry. See HMRC Brief 28/2013.

## Approach of the Courts

[4.2] For the general approach of the Courts to transactions entered into solely to avoid or reduce tax liability, leading cases are *Duke of Westminster v CIR* HL 1935, 19 TC 490; *W T Ramsay Ltd v CIR*; *Eilbeck v Rawling* HL 1981, 54 TC 101; *CIR v Burmah Oil Co Ltd* HL 1981, 54 TC 200; *Furniss v Dawson (and related appeals)* HL 1984, 55 TC 324. See also *Coates v Arndale Properties Ltd* HL 1984, 59 TC 516; *Reed v Nova Securities Ltd* HL 1985, 59 TC 516; *Magnavox Electronics Co Ltd (in liquidation) v Hall* CA 1986, 59 TC 610; *Commissioner of Inland Revenue v Challenge Corporation Ltd* PC, [1986] STC 548; *Craven v White*; *CIR v Bowater Property Developments Ltd*; *Baylis v Gregory* HL 1988, 62 TC 1; *Dunstan v Young Austen Young Ltd* CA 1988, 61 TC 448; *Shepherd v Lyntress Ltd*; *News International plc v Shepherd* Ch D 1989, 62 TC 495; *Ensign Tankers (Leasing) Ltd v Stokes* HL 1992, 64 TC 617; *Moodie v CIR and another (and related appeals)* HL 1993, 65 TC 610; *Countess Fitzwilliam and others v CIR (and related appeals)* HL 1993, 67 TC 614; *Pigott v Staines Investments Co Ltd* Ch D 1995, 68 TC 342; *CIR v McGuckian* HL 1997, 69 TC 1; *MacNiven v Westmoreland Investments Ltd* HL 2001, 73 TC 1; *CIR v Scottish Provident Institution* HL 2004, [2005] STC 15; *Mawson v Barclays Mercantile Business Finance Ltd* HL 2004, [2005] STC 1 and *HMRC v Tower Meashback LLP* SC, [2011] UKSC 19.

See also *DR Collins v HMRC* (Sp C 675), [2008] SSCD 718, *Trustees of the Eyretel Unapproved Pension Scheme v HMRC*, (Sp C 718), [2009] SSCD 17, *Mayes v HMRC* CA [2011] EWCA Civ 407; 2011 STI 1444, *Berry v HMRC* UT, [2011] STC 1057 and *Explainaway Ltd v HMRC* UT, [2012] STC 2525.

### Classical interpretation

The classical interpretation of the constraints upon the Courts in deciding cases involving tax avoidance schemes is summed up in Lord Tomlin’s statement in the *Duke of Westminster* case that ‘every man is entitled if he can to order his affairs so that the tax attaching . . . is less than it otherwise would be’. The judgment was concerned with the tax consequences of a single transaction, but in *Ramsay*, and subsequently in *Furniss v Dawson*, the House of Lords has set bounds on the ambit within which this principle can be applied in relation to modern sophisticated and increasingly artificial arrangements to avoid tax. In *CIR v McGuckian*, it was observed that while Lord Tomlin’s words in the *Duke of Westminster* case ‘still point to a material consideration, namely the general liberty of the citizen to arrange his financial affairs as he thinks fit, they have ceased to be canonical as to the tax consequences of a tax avoidance scheme’. It was further observed that the *Ramsay* principle was ‘more natural and less extreme’ than the majority decision in *Duke of Westminster*.

### The ‘Ramsay’ principle

*Ramsay* concerned a complex ‘circular’ avoidance scheme at the end of which the financial position of the parties was little changed but it was claimed that a large capital gains tax loss had been created. It was held that where a preconceived series of transactions is entered into to avoid tax and with the

clear intention to proceed through all stages to completion, once set in motion, the Duke of Westminster principle does not compel a consideration of the individual transactions and of the fiscal consequences of such transactions in isolation. The opinions of the House of Lords in *Furniss v Dawson* are of outstanding importance, and establish, *inter alia*, that the *Ramsay* principle is not confined to 'circular' devices, and that if a series of transactions is 'preordained', a particular transaction within the series, accepted as genuine, may nevertheless be ignored if it was entered into solely for fiscal reasons and without any commercial purpose other than tax avoidance, even if the series of transactions as a whole has a legitimate commercial purpose.

However, in *Craven v White* the House of Lords indicated that for the *Ramsay* principle to apply all the transactions in a series have to be preordained with such a degree of certainty that, at the time of the earlier transactions, there is no practical likelihood that the transactions would not take place. It is not sufficient that the ultimate transaction is simply of a kind that was envisaged at the time of the earlier transactions. See, however, *CIR v Scottish Provident Institution* below. In the unanimous decision of the House of Lords in *Ensign Tankers (Leasing) Ltd v Stokes*, the lead judgment drew a clear distinction between 'tax avoidance' and 'tax mitigation', it being said that the *Duke of Westminster* principle is accurate as far as the latter is concerned but does not apply to the former.

*Fitzwilliam* involved five transactions entered into over a short period of time to avoid capital transfer tax on appointments from a will trust, the last four transactions being determined by the Revenue to form a preordained series of transactions subject to the *Ramsay* principle but which the taxpayers claimed should be viewed separately with the result that by reason of a number of available reliefs no liability to capital transfer tax arose. The House of Lords stated that the correct approach to a consideration of steps 2 to 5 was to ask whether realistically they constituted a single and indivisible whole in which one or more of the steps was simply an element without independent effect and whether it was intellectually possible so to treat them. It was held that both questions should be answered in the negative. The case put by the Revenue did not depend on disregarding for fiscal purposes any one or more of steps 2 to 5 as having been introduced for fiscal purposes only and as having no independent effect, nor on treating the whole of steps 2 to 5 as having no such effect. Each of the four steps had a fiscal effect of giving rise to an income tax charge on two of the taxpayers for a period of time, and there was a potential capital transfer tax charge should either have died whilst in enjoyment of the income associated with the transactions. Although steps 2 to 5 were 'preordained', in the sense that they formed part of a pre-planned tax avoidance scheme and that there was no reasonable possibility that they would not all be carried out, the fact of preordainment in that sense was not sufficient in itself to negative the application of an exemption from liability to tax which the series of transactions was intended to create, unless the series was capable of being construed in a manner inconsistent with the application of the exemption. In the particular circumstances of the case, the series of transactions could not be so construed. Two or more transactions in the series could not be run together, as in *Furniss v Dawson*, nor could any one or more of them be disregarded. There was no rational basis on which the four separate steps

could be treated as effective for the purposes of one provision which created a charge to tax on a termination of an interest in possession but ineffective for the purposes of two other provisions which gave exemptions from that charge where the interest was disposed of for a consideration and where the interest reverted to the settlor. Accordingly, the case was one to which the *Ramsay* principle, as extended by *Furniss v Dawson*, did not apply.

In *MacNiven v Westmoreland Investments Ltd*, where the HL held that the *Ramsay* principle did not apply to a payment of interest, Lord Nicholls held that 'the very phrase "the *Ramsay* principle" is potentially misleading. In *Ramsay* the House did not enunciate any new legal principle. What the House did was to highlight that, confronted with new and sophisticated tax avoidance devices, the courts' duty is to determine the legal nature of the transactions in question and then relate them to the fiscal legislation'. Lord Hoffmann held that 'what Lord Wilberforce was doing in the *Ramsay* case was no more . . . than to treat the statutory words "loss" and "disposal" as referring to commercial concepts to which a juristic analysis of the transaction, treating each step as autonomous and independent, might not be determinative'. Lord Hutton held that 'an essential element of a transaction to which the *Ramsay* principle is applicable is that it should be artificial'.

In *Mawson v Barclays Mercantile Business Finance Ltd* the HL held that Lord Hoffmann's distinction in *Westmoreland* between 'legal' and 'commercial' concepts was not 'intended to provide a substitute for a close analysis of what the statute means'. It 'does not justify the assumption that an answer can be obtained by classifying all concepts a priori as either "commercial" or "legal"'. Instead, in applying any statutory provision, it is necessary 'first, to decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, whether the transaction in question does so'.

In *CIR v Scottish Provident Institution* the issue was whether the decision in *Craven v White* meant that a series of transactions could not be treated as a composite transaction under the *Ramsay* principle because there was a real commercial risk that the transactions would not take place. The HL held that 'it would destroy the value of the *Ramsay* principle . . . as referring to the effect of composite transactions if their composite effect had to be disregarded simply because the parties had deliberately included a commercially irrelevant contingency, creating an acceptable risk that the scheme might not work as planned'. Such a 'commercially irrelevant contingency' was found to be present in a purchased tax scheme involving options in *Schofield v HMRC CA*, [2012] STC 2019.

### Sham

In *Hitch and Others v Stone CA*, [2001] STC 214, the Revenue mounted a successful challenge to a complex and artificial tax avoidance scheme on the grounds that agreements on which it was based were shams. It was noted that 'sham' meant acts done or documents executed by the parties thereto which were intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intended to create. The law did not require that in every situation every party to the act or

## Children

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**Cross-references.** See 25.24 EXEMPTIONS AND RELIEFS for Child Trust Funds; 56.34 RESIDENCE AND DOMICILE for domicile of children.

### General

**[12.1]** There is no general bar to the chargeable gains made by an infant (i.e. an individual under 18 years of age) being assessed and charged on him personally (see *R v Newmarket Commissioners (ex p. Huxley)* CA 1916, 7 TC 49 and FA 2012, s 222(3)). HMRC can, therefore, resort directly to the infant and, for 2012/13 onwards, must do so, subject to the general legal framework for appointing people to assist those who lack capacity. Previously, there were specific tax provisions which enabled HMRC to charge and assess tax due from an infant on a guardian etc. Whether or not, in practice, they did so depended on particular circumstances.

A child is entitled to the same capital gains tax reliefs and exemptions as an adult (subject to specific exclusions).

### Nominees and bare trustees

**[12.2]** Where property is held by a person as nominee, or as trustee for any person who would be absolutely entitled against him but for being an infant, the provisions of TCGA 1992 apply as if the acts of the nominee or trustee are the acts of the infant. Acquisitions from or to the trustee or nominee to or from the infant are accordingly disregarded. References in TCGA 1992 to a person being absolutely entitled against the trustee mean that the person has the exclusive right (subject only to satisfying any outstanding charge, lien or other right of the trustee to resort to the relevant property for payment of duty, taxes, costs or other outgoings) to direct how the property shall be dealt with. [TCGA 1992, s 60]. For the wider implications of nominees and bare trustees generally, see 61.3 SETTLEMENTS.

### Assessment of guardians etc.

**[12.3]** In practice, HMRC often makes use of the machinery of TMA 1970, which enables it, for 2011/12 and earlier years, to charge and assess the tax due from an 'incapacitated person' (this term includes an 'infant': see TMA

1970, s 118), on the trustee, guardian, tutor, curator or committee, having the direction, control or management of that person's property. Such machinery applies whether or not the incapacitated person resides in the UK. The person chargeable in this way is answerable for all matters required to be done under the capital gains tax provisions, for the purpose of assessment of that tax, but is given a right of retention and indemnity in respect of tax charges or payments made on the incapacitated person's behalf. The machinery is abolished for 2012/13 onwards (see further 12.1 above). [TMA 1970, ss 72, 77; FA 2012, s 222(1)(5)].

### Default of infant

[12.4] For 2011/12 and earlier years, where the person chargeable to tax is an infant, then his parent, guardian, or tutor is liable for the tax in the event of the infant's default. On neglect or refusal of payment, the parent etc. may be proceeded against for sums due to HMRC. This provision is repealed for 2012/13 onwards. [TMA 1970, ss 73, 77; FA 2012, s 222(1)(5)].

[12.1] There is no general bar to the chargeable gains made by an infant (i.e. an individual under 18 years of age) being assessed and charged on him personally (see *R v Inwards* [1900] AC 141, 7 TC 141 and *FA 2012, s 222(1)(5)*). HMRC can, therefore, resort directly to the infant and for 2012/13 onwards, must do so, subject to the general legal framework appointing people to assist those who lack capacity. Previously, there were tax provisions which enabled HMRC to charge and assess tax due on an infant on a guardian etc. Whether or not, in practice, they did so depended on particular circumstances.

A child is treated to the same capital gains tax rules and exemptions as an adult (subject to specific exclusions).

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[12.2] Where property is held by a person as nominee or as trustee for any person who would be absolutely entitled against him but for being an infant, the provisions of TCGA 1992 apply as if the acts of the nominee or trustee are the acts of the infant. Acquisitions from or to the trustee or nominee to or from the infant are accordingly dateable. References in TCGA 1992 to a person being absolutely entitled against the trustee mean that the person has the exclusive right (subject only to existing tax outstanding charge, lien or other right of the trustee to resort to the relevant property for payment of duty, taxes, costs or other outgoings) to direct how the property shall be dealt with. (TCGA 1992, s 60]. For the wider implications of nominees and bare trustees generally, see 61.3 SETTLEMENTS.

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## Claims

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Cross-reference. See 43.4 LOSSES for requirement to notify capital losses.

### Introduction

[13.1] This chapter outlines the procedures and time limits for making claims and elections for reliefs, allowances and tax repayments for both capital gains tax and corporation tax purposes.

Claims are personal matters and (except in the case of trustees for persons under disability etc.) can be made only by the person entitled to the relief (cf. *Fulford v Hyslop* Ch D 1929, 8 ATC 588). See 57.4 RETURNS for the signing of claims by an attorney.

Also covered in this chapter are two specific types of claim:

- (a) claims for recovery of overpaid tax (previously 'error or mistake' relief); and
- (b) claims through the courts for the restitution of payments made under a mistake of law.

### Capital gains tax claims and elections

[13.2] A formal procedure applies to the making of capital gains tax (and income tax) claims, elections and notices. A claim for a relief, allowance or tax repayment must be for an amount quantified at the time of the claim. Where notice has been given by HMRC requiring the delivery of a return (see 57.3, 57.16 RETURNS), a claim etc. can only be made at any time by inclusion in such a return (or by virtue of an amendment to a return) *unless it could not be so included* either at that time or subsequently (but see below for claims involving two or more years). These provisions do not apply to claims to be given effect

by a PAYE coding adjustment, to claims by charities for specified exemptions and repayments of income tax, or to claims for consequential adjustments after the counteraction of a tax advantage under the GAAR (see 4.3 ANTI-AVOIDANCE).

In the case of a partnership business, a claim under any of numerous provisions specified in TMA 1970, s 42(7) must be made by a partner nominated by the partnership if it cannot be included in a partnership return (or amendment to such a return). See 13.3 below for provisions applying where a claim etc. is made otherwise than by inclusion in a return.

Where a claimant discovers that an error or mistake has been made in a claim (whether or not made in a return), he may make a supplementary claim within the time allowed for making the original claim.

[TMA 1970, s 42; FA 2010, Sch 8 para 4; FA 2012, s 222(1), Sch 15 paras 11, 17(6); FA 2013, s 213].

#### Claims for relief involving two or more years

A claim for a loss incurred or payment made in one tax year to be carried back to an earlier year or years need not be made in a return, is treated as a claim for the year of loss or payment (the later year), must be for an amount equal to what would otherwise have been the tax saving for the earlier year, and is given effect *in relation to the later year* by repayment, set-off etc. or by treating the said amount as a tax payment made on account under SELF-ASSESSMENT (60.2). The tax position for the earlier year is not adjusted. [TMA 1970, Sch 1B para 2]. See Tolley's Income Tax for more details. The non-reopening of the earlier year's self-assessment does not prevent the making or revising of other claims for that earlier year that are consequential to the carry-back (Revenue Tax Bulletin August 2000 pp 774, 775). In relation to the carry-back claim, repayment interest or (before 31 October 2011) repayment supplement may be due as in 55.2, 55.3 REPAYMENT INTEREST, though only from 31 January following the *later year* (as above). An example of a capital gains provision affected by these rules is the potential three-year carry-back of capital losses incurred by an individual in the tax year in which he dies — see 19.7 DEATH.

#### Claims etc. not included in returns

[13.3] Subject to any specific provision requiring a claim, etc. to be made to the Commissioners for HMRC, an income tax or capital gains tax claim or election made otherwise than in a return (see 13.2 above) must be made to an officer of Revenue and Customs. The claim, etc. must include a declaration by the claimant that all particulars are correctly stated to the best of his information or belief. No claim requiring a tax repayment can be made unless the claimant has documentary proof that the tax has been paid or deducted. The claim must be made in a form determined by HMRC and may require, inter alia, a statement of the amount of tax to be discharged or repaid and supporting information and documentation. In the case of a claim by or on behalf of a person who is not resident (or who claims to be not resident or not domiciled or, for 2012/13 and earlier years, not ordinarily resident) in the UK, HMRC may require a statement or declaration in support of the claim to be made by affidavit.

A person who may wish to make a claim must keep all such records as may be requisite for the purpose and must preserve them until such time as HMRC may no longer enquire into the claim (see below) or any such enquiry is completed. HMRC have the power to make regulations specifying records which are required to be kept. There is a maximum penalty of £3,000 for non-compliance in relation to any claim actually made. Similar provisions and exceptions apply as in 57.8 RETURNS as to the preservation of copies of documents instead of originals.

Provisions similar to those in 57.7 RETURNS (amendments of self-assessments) apply to enable a claimant (within twelve months of the claim) or HMRC officer (within nine months of the claim) to amend a claim etc. HMRC has power of enquiry into a claim, etc. (or amendment) similar to that in 57.9 RETURNS (enquiries into returns). Notice of intention to enquire must be given by the first anniversary of 31 January following the tax year (or where the claim relates to a period other than a tax year, the first anniversary of the end of that period) or, if later, the quarter day (meaning 31 January, 30 April, etc.) next following the first anniversary of the date of claim, etc. See also 34.3–34.10 HMRC INVESTIGATORY POWERS. Where an enquiry is in progress, an HMRC officer may give provisional effect to the claim, etc. (or amendment thereof) to such extent as he thinks fit. Provisions similar to those in 57.12, 57.13 RETURNS apply as regards completion of enquiries and amendments of claims upon completion. HMRC must give effect (by assessment, discharge or repayment) to an amendment arising out of an enquiry within 30 days after the date of issue of the closure notice. An appeal may be made against any conclusion stated, or amendment made, by a closure notice by giving written notice to the relevant officer within 30 days after the date of issue of the closure notice, extended to three months where certain specified issues concerning residence are involved. If an amendment is varied on appeal, HMRC must give effect to the variation within 30 days.

Where a claim etc. does not give rise to a discharge or repayment of tax, there are provisions for disallowance of the claim on completion of enquiry, with appeal procedures similar to those above.

[TMA 1970, s 42(11), Sch 1A; SI 2009 No 402; SI 2009 No 56, Sch 1 paras 53–58; FA 2013, Sch 46 para 117; SI 2009 No 2035, Sch para 9].

In *Cotter v HMRC SC*, [2013] STC 2480 a claim for loss relief which was included in a tax return form was held to be made outside the return and therefore subject to the enquiry provisions above. For the purposes of the enquiry provisions, a tax return referred to the information in the return form which was submitted for the purpose of establishing the amounts in which a person was chargeable to tax for the relevant tax year. In this case, the claim had no effect on the tax chargeable for the year concerned and so did not form part of the tax return.

#### Corporation tax claims

[13.4] Under corporation tax self-assessment, provisions having broadly similar effect as those in 13.2 above (other than those of TMA 1970, Sch 1B) apply to companies. Subject to any express provision to the contrary and

[TMA 1970, ss 43A, 43B].

Where HMRC issue an amendment to a return as part of an enquiry closure notice (see 57.12 RETURNS), these provisions apply to the amendment as they apply to assessments. [TMA 1970, s 43C(2)(3)].

The provisions broadly apply to companies under corporation tax self-assessment. [FA 1998, s 117, Sch 18 paras 61–64].

#### Extended time limits for assessment

Where it is necessary to make an assessment on any person to give effect to, or as a result of allowing, a claim, supplementary claim, election, application or notice given or made under the extended time limits of TMA 1970, ss 36(3), 43(3), 43A or 43C above, the assessment is not out of time if made within one year of the final determination of the claim etc. For this purpose a claim etc. is finally determined when it can no longer be varied, on appeal or otherwise. [TMA 1970, s 43C(4)(5); TIOPA 2010, Sch 8 para 6].

#### Appeals in respect of claims

[13.6] See 13.3 above and 5.2 APPEALS.

#### Claim for recovery of overpaid tax

[13.7] A claim under the following provisions can be made on or after 1 April 2010. The provisions replace the narrower error or mistake relief provisions, for which see the 2013/14 or earlier edition of this work. A claim to the special relief described below can be made on or after 1 April 2011; the relief replaces HMRC's concessional practice of 'equitable liability' — see 50.25 PAYMENT OF TAX.

Where a taxpayer has paid an amount of capital gains tax (or income tax) or corporation tax and believes that the tax is not due, he can make a claim to HMRC for repayment of the tax. Where a taxpayer has been assessed as liable to pay an amount of tax, or there has been a determination or direction to that effect, he can likewise make a claim for the amount to be discharged if he believes that the tax is not due. For these purposes, tax paid by one person on behalf of another is treated as paid by the other person.

HMRC will not give effect to such a claim in the following circumstances:

- (a) the amount is excessive because of a mistake in a claim or a mistake consisting of making, or failing to make, an election claim or notice (or because of certain mistakes relating to capital allowances);
- (b) the claimant can seek relief by taking other steps under tax legislation;
- (c) the claimant could have sought relief by taking such steps within a period which has expired by the time the claim is made, if he knew, or ought reasonably to have known, before the end of that period that such relief was available;

- (d) the claim is made on grounds that have been put to a court or tribunal in the course of an appeal relating to the amount or grounds that have been put to HMRC in the course of such an appeal settled by agreement;
- (e) the claimant knew, or ought reasonably to have known, of the grounds for the claim before the latest of: the date an appeal relating to the amount was determined by a court or tribunal, the date on which such an appeal was withdrawn by the claimant, and the end of the period in which the claimant could have appealed;
- (f) the amount was due as a result of proceedings by HMRC against the claimant, or under an agreement between the claimant and HMRC settling such proceedings; and
- (g) the amount is excessive because of a mistake in calculating the claimant's liability where the liability was calculated in accordance with the practice generally prevailing at the time (and for this purpose special rules apply in relation to PAYE).

The exclusion in (g) above does not apply where a claim to relief relates to tax charged contrary to EU law. For this purpose, an amount is charged contrary to EU law if it is contrary to the provisions of the Treaty on the Functioning of the European Union relating to the free movement of goods, persons, services or capital (or replacement provisions under any subsequent treaty). This rule is made statutory for claims made on or after 17 January 2014 but was previously applied by HMRC in accordance with HMRC Brief 22/10.

[TMA 1970, s 33, Sch 1AB paras 1, 2; FA 1998, Sch 18 paras 51, 51A; FA 2013, s 231(1)(3)(5)].

#### Making a claim

For capital gains tax (and income tax) purposes, a claim must be made within four years after the end of the tax year concerned. Where the claim relates to tax overpaid, that year is the year in respect of which the payment was made or, where the amount paid is excessive due to a mistake in a tax return or returns, the year to which the return (or if more than one, the first return) relates. Where the claim relates to an assessment, determination or direction, the year concerned is the year to which that assessment etc. relates or, for claims made on or after 17 January 2014 where the amount due is excessive due to a mistake in a tax return or returns, the year to which the return (or if more than one, the first return) relates. The time limit is extended for claims relating to mistakes in returns made before 1 April 2012 by a person other than a company if the return was not issued within one year of the end of the tax year to which it relates. In such cases, the claim must be made within five years after the 31 January following the end of the tax year concerned.

For corporation tax purposes, a claim must be made within four years after the end of the accounting period concerned. Where the claim relates to tax overpaid, that accounting period is the period in respect of which the payment was made or, where the amount paid is excessive due to a mistake in a tax return or returns, the period to which the return (or if more than one, the first return) relates. Where the claim relates to an assessment, determination or direction, the accounting period concerned is that to which that assessment etc.

Following FA 2013, chargeable gains arising on EMI shares are now eligible for entrepreneurs' relief – see 24.6.

#### Rights issues

If there is a rights issue affecting qualifying shares, the share reorganisation rules of TCGA 1992, ss 127–130 (see 62.2 SHARES AND SECURITIES) are disapplied, with the result that the rights shares are treated as a separate acquisition and are not qualifying shares.

[TCGA 1992, Sch 7D paras 14, 16].

#### Identification rules

For an election to modify the normal rules in a case where EMI scheme shares are acquired on the same day as other shares in the same company, see 63.2 SHARES AND SECURITIES — IDENTIFICATION RULES.

### Other tax-advantaged share option schemes

[22.23] The following apply generally to other tax-advantaged share option schemes (see 22.24 onwards below).

#### Assignment, release or abandonment of tax-advantaged employee share option

The same comments apply as for unapproved options at 22.7 above.

#### Identification rules

For an election to modify the normal rules in a case where approved share option scheme shares are acquired on the same day as other shares in the same company, see 63.2 SHARES AND SECURITIES — IDENTIFICATION RULES.

#### Save as you earn (SAYE) share option schemes

[22.24] Under a SAYE share option scheme, a company grants to an employee of itself or its group an option to acquire ordinary shares in the company at a specified price (the option price) at a specified future date. No income tax charge arises on either the grant of the option or, on exercise of the option, on any excess of the then value of the shares over the option price. The option price must not be less than 80% of the market value of shares of the same class at the time the option is granted. The scheme is linked to an approved certified contractual savings (CCS) scheme with a bank, building society or other authorised provider, to which the employee makes regular contributions by deduction from salary and to which a tax-free bonus is added at maturity (the bonus date), the funds then being used to purchase the agreed number of shares at the option price (though the funds may alternatively be repaid to the employee if he so chooses, the option being allowed to lapse). Savings contracts of between three years and five years are available, and five-year contracts may offer the choice of an extension to seven years.

Aggregate monthly contributions to all such schemes to which an employee contributes at any one time cannot exceed £250, and the minimum monthly contribution set for any scheme must not exceed £10 (although monthly contributions as low as £5 are permitted).

Other than in specified circumstances, the option cannot be exercised before the bonus date, nor can it be exercised, except in the case of death (for which special rules apply), more than six months after that date. The circumstances under which early exercise may be permitted include *inter alia* (i) the takeover of the company whose shares are scheme shares, (ii) where the eligible employment is in a subsidiary company, the company which established the scheme ceasing to have control of that subsidiary, and (iii) the transfer (to a person other than a subsidiary or associated company) of the business (or part thereof) to which the employment relates. In each case, the option can be exercised within six months of the change but if, in any of these three instances, the option is thus exercised within three years of its being granted, the income tax exemption on exercise is lost and a charge may arise under ITEPA 2003, s 476 (see 22.6 above); the income tax exemption on the grant of the option does, however, continue to apply.

The scheme must be available on similar terms (subject to any variations by reference to salary level, period of service etc.) to all employees and full-time directors within ITEPA 2003, s 15 (for 2007/08 and earlier years, ITEPA 2003, ss 15 or 21) and with a stipulated minimum period of service, which cannot be more than five years. It may be made available to other employees and directors. Where the company is a close company, those with material interests are excluded.

[ITEPA 2003, ss 516–520, Sch 3; FA 2013, Sch 2 paras 7–13, 39–43; FA 2014, Sch 8 paras 97–157, Sch 37 para 20].

With effect from 6 April 2014 a number of changes are to be made to these provisions. The maximum monthly contribution is to increase to £500 with effect from 6 April 2014. (Autumn Tax Update 2013).

See Tolley's Income Tax for the full provisions and conditions.

#### Capital gains tax

Other than where early exercise of the option results in the loss of the income tax exemption as mentioned above (in which case see 22.6 above), the provisions of TCGA 1992, s 17 (see 44.1 MARKET VALUE) are specifically disapplied both in calculating the CGT acquisition cost of the shares to the employee and for the purposes of any corresponding disposal to him. Those provisions are likewise disapplied where an option is exercised following the death of the employee in accordance with a rule included in the scheme by virtue of ITEPA 2003, Sch 3 para 32. [TCGA 1992, Sch 7D para 10; FA 2014, Sch 8 para 128].

On a disposal of the shares by the employee, his allowable expenditure consists of the actual consideration given on the exercise of the option, i.e. the amount saved plus the tax-free bonus (plus, if applicable, any consideration given for the option itself — see 22.3 above). The date of acquisition of the shares for CGT purposes is the date the option is exercised.

Shares acquired through an approved SAYE share option scheme may be transferred without CGT consequences to an Individual Savings Account (see 25.30 EXEMPTIONS AND RELIEFS), subject to the annual subscription limits (applied by reference to market value transferred) and provided the transfer is made within 90 days after the option is exercised.

### Company share option plan (CSOP) schemes

[22.25] CSOP schemes were introduced by FA 1996 to replace executive share option schemes (see 22.27 below). Unlike SAYE share option schemes and profit sharing schemes, company share option plans and their predecessors are not required to be open to all employees, and are more likely to be used to reward directors and key employees. CSOP schemes are more restrictive than their predecessors in that they place a lower ceiling on the value of options an individual may hold at any one time and do not permit the option price to be discounted by reference to the current share price.

Under a CSOP scheme, a company grants to an employee of itself or its group an option to acquire ordinary shares in the company at a specified price (the option price) at a specified future date. The option price should not be less than the market value of the shares at the time of the grant. Normally, no income tax charge arises on either the grant of the option or, on exercise of the option, on any excess of the then value of the shares over the option price. In the exceptional case where the aggregate of the option price and any amount paid for the option itself is less than the market value of the shares at the time of the grant, the amount of the difference counts as employment income for the tax year in which the option is granted. The normal tax exemption on exercise of the option does not apply if the scheme is no longer a tax-advantaged scheme at the time of exercise or if the option is exercised less than three years or more than ten years after it was granted. There is an exception for options exercised within three years of grant but no later than six months after the individual ceases to be a qualifying employee of the scheme organiser (or of a constituent company in a group scheme) because of injury, disability, redundancy or retirement. Special rules apply in cases of death.

Only full-time directors (generally taken to mean those working at least 25 hours per week) are eligible. Part-time employees (other than directors) may be included. Where the company is a close company, employees and directors with material interests are excluded.

It is a condition of approval that the aggregate market value (at the time of grant) of shares over which an individual may hold unexercised rights under the scheme (and any other CSOP scheme established by the company or an associated company) must at no time exceed £30,000.

[ITEPA 2003, ss 521–526, Sch 4; FA 2010, s 39; FA 2013, Sch 2 paras 14, 15, 44; FA 2014, Sch 8 paras 50, 158–215, Sch 37 para 21].

See Tolley's Income Tax for the full provisions and conditions.

### Capital gains tax

Where the income tax exemption on exercise of the option applies (see above), the provisions of TCGA 1992, s 17 (see 44.1 MARKET VALUE) are specifically disapplied both in calculating the CGT acquisition cost of the shares to the

employee and for the purposes of any corresponding disposal to him. Those provisions are likewise disapplied where an option is exercised following the death of the employee in accordance with a rule included in the scheme by virtue of ITEPA 2003, Sch 4 para 25. [TCGA 1992, Sch 7D para 13; FA 2014, Sch 8 para 189].

Where, exceptionally, an income tax liability arises on the grant of the option (due to the option price being discounted — see above), the amount counted as employment income is included in the cost of acquisition of the shares for CGT purposes. This applies whether or not the exercise is in accordance with the provisions of the scheme and whether or not the scheme is still approved at the time of the exercise. [TCGA 1992, s 120(2)(6)(c), Sch 7D para 12; FA 2014, Sch 8 para 188].

Thus, on a disposal of the shares by the employee, his allowable expenditure within TCGA 1992, s 38(1)(a) (see 16.11(a) COMPUTATION OF GAINS AND LOSSES) consists of:

- the actual consideration given on the exercise of the option,
- any consideration given for the option itself, and
- the amount, if any, counting as employment income.

The date of acquisition of the shares for CGT purposes is the date the option is exercised. Any deemed expenditure corresponding to an amount chargeable to income tax is also deemed to have been incurred on that date.

### Employee shareholder shares

[22.26] A special employment status, known as 'employee shareholder' status, was introduced by Growth and Infrastructure Act 2013, s 31. Employee shareholders are issued or allotted at least £2,000 worth of shares in consideration of an employee shareholder agreement. Subject to conditions, an income tax relief and capital gains tax exemption apply to the shares, as described below. The relief and exemption apply to shares received through the adoption of employee shareholder status on or after 1 September 2013. [FA 2013, Sch 23 para 38; SI 2013 No 1755]. Businesses wishing to award shares under an employee shareholder agreement may propose a share valuation to HMRC's Shares and Assets Valuation team in advance of the award (HMRC Employment-Related Shares & Securities Bulletin No. 10, September 2013). For official guidance on employee shareholder status see [www.hmrc.gov.uk/employee-shareholder/index.htm](http://www.hmrc.gov.uk/employee-shareholder/index.htm).

### Charge to income tax

When shares ('employee shareholder shares') with a market value of at least £2,000 are acquired by an employee in consideration of an 'employee shareholder agreement', an amount is treated as earnings from the employment, in respect of the acquisition of the shares, for the tax year in which they are acquired. The amount is found by applying a formula,  $MV - P$  where:

$MV$  = the market value of the shares (see below) on the day on which they are acquired; and

P = the payment (if any) that the employee is treated as having made for the shares as set out below.

If P exceeds MV, the amount is nil.

Where the above applies, no other sums can constitute earnings from the employment in respect of the acquisition of the employee shareholder shares.

Market value is determined as for capital gains purposes.

An 'employee shareholder agreement' means an agreement by virtue of which an employee is an employee shareholder (see *Employment Rights Act 1996, s 205A(1)(a)-(d)*). Shares are acquired by an employee for these purposes if the employee becomes beneficially entitled to them; they are acquired at the time when the employee becomes so entitled.

#### Deemed payment for the shares

Provided that, as above, shares with a market value of at least £2,000 are acquired by an employee in consideration of an employee shareholder agreement, the employee is treated, for income tax purposes, as having made a payment for those shares as follows. Where all the shares acquired in consideration of the agreement are acquired on the same day, the employee is treated as having made on that day a payment of £2,000 for those shares. Where shares are acquired by the employee in consideration of the agreement on more than one day, with shares with a market value of at least £2,000 acquired on the first of those days, the employee is treated as having made, on the first of those days, a payment of £2,000 for the shares acquired on that day. Where shares with a value in excess of £2,000 are acquired, the payment which the employee is treated as having made for each share is determined on a pro rata basis.

Except as provided above, the employee is to be treated for income tax purposes as having given no consideration for shares acquired in consideration of the employee shareholder agreement.

See Tolley's Income Tax for the full provisions and conditions.

[ITEPA 2003, ss 226A-226D; FA 2013, Sch 23 paras 1-3].

#### Capital gains tax

Gains on 'exempt' employee shareholder shares are not chargeable gains when the shares are disposed of by the person who acquired them under the employee shareholder agreement. An employee shareholder share acquired in consideration of an employee shareholder agreement is 'exempt' if, immediately after its acquisition, the total value of employee shareholder shares, in the employer company or an 'associated company', which have been acquired by the employee does not exceed £50,000. For these purposes, the value of a share at any time is its unrestricted market value at the time when it was acquired by the employee. Where shares acquired on a particular day take an employee over the £50,000 limit, an apportionment is made to treat the appropriate proportion up to the limit (rounded down to the nearest share) as acquired before the remainder (and so as exempt shares).

For these purposes, a company is an associated company of another if one has control of the other or both are under the control of the same person(s). 'Control' is construed in accordance with *CTA 2010, ss 450, 451*. If a company controls another when an employee shareholder agreement is entered into with an employee, this is treated as continuing to be the case when any subsequent employee shareholder agreement is entered into with that same employee. However, this does not apply if:

- one of the two companies has been dissolved;
- two years have passed since the date of dissolution; and
- the employee has not, at any time in that two-year period, been engaged in any office or employment (including engagement under a contract for services) with any company which is an associated company of the dissolved company.

An employee shareholder share is not exempt if:

- on the date on which the share is acquired or at any time in the twelve months ending on that date, the employee has (or has had) a 'material interest' in the employer company or a parent undertaking (within *Companies Act 2006, s 1162*) of the employer company; or
- on the date on which the share is acquired, the employee is connected (within 17 CONNECTED PERSONS) with an individual who has a material interest in the employer company or a parent undertaking or who has had such an interest at any time in the twelve months ending on that date.

For these purposes, an individual (A) has a 'material interest' in a company if at least 25% of the voting rights are exercisable by A, or by persons connected with A, or by A and persons connected with A together. If the company is a close company, or would be but for being a non-UK resident company or a quoted company, A has a material interest in it if A, or persons connected with A, or A and persons connected with A together, are entitled to at least 25% of the assets available for distribution among the participators in a winding-up or in any other circumstances. A is treated as having a material interest in a company at any time if A, or persons connected with A, or A and persons connected with A together, have an entitlement to acquire such rights as would (together with any existing rights) give A a material interest in the company. Any arrangements in place (as widely defined and to which the employer company or a parent undertaking is also party) to acquire such rights must also be taken into account.

Where an individual has acquired shares in consideration of entering into an employee shareholder agreement, he is not regarded as disposing of an asset by reason of ceasing to have, or not acquiring, the rights mentioned in *Employment Rights Act 1996, s 205A* as a result of entering into the agreement.

#### Identification rules

The normal identification rules (see 63.2 SHARES AND SECURITIES — IDENTIFICATION RULES) are each disapplied as regards exempt employee shareholder shares. Where an employee holds shares of the same class in a company and only some of those shares are exempt employee shareholder shares, on a disposal of a part

- SP 4/01 **Double taxation conventions with the former USSR and with newly independent states.** The position is updated, superseding SP 3/92 above. See 21.2 DOUBLE TAX RELIEF.
- SP 5/01 **Corporation tax self-assessment: claims to loss relief, capital allowances and group relief made outside the normal time limit.** The circumstances in which HMRC will exercise their discretion with regard to such late claims are explained. See 57.19 RETURNS.
- SP 1/02 **Corporation tax self-assessment enquiries.** Where an enquiry into a corporation tax return remains open pending agreement of a chargeable gains valuation, HMRC will not use the open enquiry to raise new issues which they would not otherwise have been able to raise. See 57.19 RETURNS.
- SP 3/02 **Financial futures and options.** HMRC's views on the tax treatment of transactions in certain financial futures and options, with particular reference to whether such transactions are to be regarded as profits or losses of a trade or taxed under the chargeable gains rules. Replaces SP 14/91. See 7.7, 7.8 ASSETS.
- SP 5/02 **Exemption for substantial shareholdings of companies.** HMRC guidance on the application of the anti-avoidance rule at 65.6 SUBSTANTIAL SHAREHOLDINGS OF COMPANIES.
- SP 2/04 **Allowable expenditure: expenses incurred by personal representatives and corporate trustees under TCGA 1992, s 38(1)(b).** For deaths after 5 April 2004, a revised scale of expenditure is allowable for costs of establishing title in computing gains or losses of personal representatives on the sale of assets in a deceased person's estate. See 19.10 DEATH.
- SP 3/04 **Double taxation convention with the former Yugoslavia.** The position is updated, superseding SP 6/93 above. See 21.2 DOUBLE TAX RELIEF.
- SP 1/06 **Self-assessment — finality and discovery.** HMRC set out their views on finality of self-assessments and discovery following the decision in *Veltema v Langham*. See 6.5 ASSESSMENTS.
- SP 2/06 **Venture capital trusts, EIS and corporate venturing scheme: value of gross assets.** HMRC set out their approach in applying the 'gross assets requirement'. Replaces SP 2/00. See 18.7 CORPORATE VENTURING SCHEME, 23.5 ENTERPRISE INVESTMENT SCHEME, and 70.4 VENTURE CAPITAL TRUSTS.
- SP 3/07 **Double taxation convention with the former Yugoslavia.** The position is updated, superseding SP 3/04. See 21.3 DOUBLE TAX RELIEF.

## Hold-Over Reliefs

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Simon's Taxes. See C1.425–C1.428, C3.5.

### Introduction

[36.1] There are currently two separate hold-over reliefs which apply to:

- disposals by individuals or trustees of business assets where the disposal is not at arm's length (for example, gifts); and
- disposals by individuals or trustees in respect of which inheritance tax is chargeable (or would be but for certain exemptions).

The effect of the reliefs is to reduce or eliminate the chargeable gain on the disposal and to make a corresponding reduction in the acquisition cost of the transferee. Relief must be claimed, usually by way of a joint claim by both transferor or transferee. Relief is denied in certain circumstances, including where the transferee is not UK-resident nor ordinarily resident or is the trustee of a settlor-interested settlement. Relief already given is also clawed back in certain circumstances, including where the transferee subsequently emigrates. See 36.8 and 36.11 below.

The current restricted hold-over reliefs replaced wider reliefs in 1989. These superseded reliefs are described briefly at 36.9 and 36.12 below for their possible ongoing effect on acquisition costs.

### Relief for gifts of business assets

[36.2] The hold-over relief described below applies where:

- an individual (*'the transferor'*) makes a disposal not at arm's length (e.g. a gift) of an asset specified below, and
- a joint claim for relief is made by him and the transferee, or, where the transferee is a trustee of a settlement, by him alone.

[TCGA 1992, s 165(1)].

Note that the transferee need not be an individual and may, for example, be a company. See also 36.5 below re agricultural property and 36.6 below re settled property.

An asset is within (a) above if:

- it is, or is an interest in, an asset used for the purposes of a trade, profession or vocation carried on by the transferor, his 'personal company' or a member of a 'trading group' of which the 'holding company' is his personal company), or
- it consists of shares or securities of a 'trading company', or of the holding company of a trading group, where *either* the shares etc. are neither listed on a recognised stock exchange (within ITA 2007, s 1005 — see 62.31 SHARES AND SECURITIES) nor dealt in on the Unlisted Securities Market (now closed) *or* the trading company or holding company is the transferor's personal company.

[TCGA 1992, s 165(2)].

Hold-over relief does not apply on a disposal if:

- the disposal is a transfer of shares or securities and the transferee is a company;
- the gain arises by virtue of TCGA 1992, s 116(10)(b) (disposal of qualifying corporate bonds derived from shares giving rise to deferred gain, see 53.4 QUALIFYING CORPORATE BONDS); *or*
- hold-over relief is available (or would be if a claim were made) under TCGA 1992, s 260 in 36.10 below for gifts on which inheritance tax is chargeable etc.

[TCGA 1992, s 165(3)].

See also the restriction and clawback provisions in 36.8 below.

### Definitions

[36.3] For the purposes of 36.2 above, an individual's 'personal company' is a company the voting rights in which are 'exercisable', as to not less than 5%, by that individual. ('Exercisable' means capable of being exercised, whether or not in fact exercised (*Hepworth v Smith* Ch D 1981, 54 TC 396).)

'Trading group', 'holding company' and 'trading company' have the following meanings. For the purposes of the definitions, the activities of group members are regarded as a single business, so that intra-group activities are disregarded.

A 'trading group' is a 'group of companies' (see below), one or more of whose members carry on 'trading activities' and the activities of whose members, taken together, do not include to a 'substantial' extent activities other than trading activities. 'Trading activities' means activities carried on by a member of the group being activities that would fall within (A)–(D) below if these are interpreted by reference not only to that member but also to any other member of the group. A group member acquires a 'significant interest' (see (D) below) if it requires sufficient ordinary share capital in the other company to make that company a member of the same group as the acquiring company, or to give the acquiring company a qualifying shareholding in a 'joint venture company'. In determining whether a group of companies is a trading group, there is disregarded any 'qualifying shareholding' held by any member of the group in a 'joint venture company'. Each such member is regarded as carrying on a share of the joint venture company's activities (or, if the joint venture company is itself a holding company of a trading group, a share of that group's activities) proportionate to its percentage shareholding in that company. This does not apply if the joint venture company is itself a member of the group.

The views expressed in HMRC's Capital Gains Manual on the meaning of 'trading company' (see below) are also of relevance to 'trading groups', but intra-group activities are disregarded in applying the various tests (HMRC Capital Gains Manual CG17953f).

A 'group of companies' means a company and its '51% subsidiary(ies)' (within CTA 2010, Pt 24 Ch 3).

A 'holding company' is a company with one or more 51% subsidiaries.

A 'trading company' is a company carrying on 'trading activities' whose activities do not include to a 'substantial' extent activities other than trading activities. 'Trading activities' means 'activities' carried on by the company:

- in the course of, or for the purposes of, a 'trade' being carried on by it; *or*
- for the purposes of a trade that it is preparing to carry on; *or*
- with a view to its acquiring or starting to carry on a trade; *or*
- with a view to its acquiring a 'significant interest' in the share capital of another company that is itself a trading company or the holding company of a trading group and that is not already a member of the same group as the acquiring company (where applicable).

'Activities' is interpreted by HMRC to mean what a company does, and thus the expression in itself includes engaging in trading activities, making and holding investments, planning, holding meetings and so forth (HMRC Capital Gains Manual CG17953). Activities qualify under (C) or (D) above only if the acquisition is made, or the trade commenced, as soon as reasonably practicable in the circumstances. A company acquires a 'significant interest' (see (D) above) if it acquires sufficient ordinary share capital in the other company to make that company its 51% subsidiary (within CTA 2010, Pt 24 Ch 3), or to give the acquiring company a qualifying shareholding in a joint venture company without making the two companies members of the same group. For further interpretation of (A)–(D) above, see HMRC Capital Gains Manual CG17953i–17953l.

In determining whether a company with a qualifying shareholding in a joint venture company is a trading company, any holding of shares by it in the joint venture company is disregarded. It is regarded as carrying on a share of the joint venture company's activities proportionate to its percentage shareholding in that company.

For the purposes of the above definitions (but not for the general purposes of the above relief — see below) 'trade' means a trade, profession or vocation, as understood for income tax purposes, which is conducted on a commercial basis with a view to realisation of profits. The expression also expressly includes the commercial letting of FURNISHED HOLIDAY ACCOMMODATION (26), but other letting of furnished property is excluded (*Patel v Maidment Sp C 2003* [2004] SSCD 41, Sp C 384).

A 'joint venture company' is a company:

- (I) which is a trading company or the holding company of a trading group, and
- (II) at least 75% in aggregate of the ordinary share capital (within ITA 2007, s 989) of which is held by no more than five persons (counting shares held by different members of a group of companies as held by a single company).

A company has a 'qualifying shareholding' in a joint venture company if:

- it holds 10% or more of the ordinary share capital of the joint venture company, or
- (where the company is a member of a group of companies) the company and the other members of the group between them hold 10% or more of that ordinary share capital.

In interpreting the above, HMRC take 'substantial' to mean 'more than 20%'. Depending on the facts of the case, this measure may be applied to turnover, expenditure and/or time spent by officers and employees where one or more of these items relate partly to non-trading activities, and/or to non-trading assets as a proportion of all assets (either of which may possibly include intangible assets such as goodwill). The fact that a company has investment income does not necessarily bring the 20% test into play. If it can be shown that holding the investment is integral to the conduct of the trade or is a short-term lodgement of surplus funds held to meet demonstrable trading liabilities, the investment

is unlikely to be seen as evidence of a non-trading purpose. An investment outside these categories still has the safety net of the 20% test. As regards property owned by the company but surplus to immediate business requirements, HMRC do not necessarily regard any of the following as indicating a non-trading purpose:

- letting part of the trading premises;
- letting properties no longer required for the trade and intended to be sold eventually;
- subletting property where it would be impractical or uneconomic to assign or surrender the lease;
- acquiring property, whether vacant or already let, with the provable intention of bringing it into use for the purpose of the trade.

In establishing 'purposes' under the old definition, only those reflected in the company's actual, or seriously contemplated, activities are to be taken into account and not, for example, myriad activities theoretically available to the company under wide powers conferred by its articles of association.

'Trade', 'profession' and 'vocation' generally have the same meanings as in the *Income Tax Acts* but any UK property business which consists of, or so far as it consists of, the commercial letting of FURNISHED HOLIDAY ACCOMMODATION (26) in the UK is treated as a trade for relief purposes. Similarly (and subject to what is said at 26.1 FURNISHED HOLIDAY ACCOMMODATION), any overseas property business which consists of, or so far as it consists of, the commercial letting of such accommodation in one or more EEA states is treated as a trade. In determining whether for these purposes a company is a trading company, a 'trade' includes the occupation of woodlands managed on a commercial basis by the occupier with a view to profit.

[TCGA 1992, ss 165(8)(9), 165A, 241(3)(3A), 241A(4)(5); FA 2011, Sch 14 para 14(3)].

### Nature of relief

[36.4] Where there is no actual consideration for the disposal (as opposed to a deemed MARKET VALUE (44.1) consideration under TCGA 1992, s 17(1)), or where an actual consideration does not exceed the allowable expenditure within TCGA 1992, s 38 (see 16.11 COMPUTATION OF GAINS AND LOSSES) relating to the asset, the effect of a claim is that the gain otherwise chargeable on the transferor and the transferee's acquisition cost are each reduced by the 'held-over gain'.

The 'held-over gain' for this purpose is the gain otherwise chargeable (termed the 'unrelieved gain') but subject to the reductions described below. Where actual consideration exceeds the allowable expenditure, the held-over gain is the unrelieved gain less that excess (see the *example* at 36.7 below) but again subject to the reductions below. (*Note.* Indexation allowance, where available, is deductible in arriving at the gain otherwise chargeable but it is not allowable expenditure within TCGA 1992, s 38.)

[TCGA 1992, s 165(4)(6)(7)].

**Order of set-off**

Losses arising to individuals, trustees and personal representatives in the year 1996/97 and subsequent years are to be treated as utilised before losses arising in earlier years. Similarly, losses accruing to companies for accounting periods ending on or after 1 July 1999 will have preference to losses arising in accounting periods ending before that date. [FA 1995, s 113(2)].

**Carry-back prohibited**

[43.5] Losses may not normally be carried back against the gains of an earlier year. There are two exceptions to this rule. See 19.7 DEATH for carry-back of losses from the year of death and 43.19 below for the election to treat a loss on a right to unascertainable consideration as accruing in an earlier year.

**Connected persons**

[43.6] A loss on a disposal to a CONNECTED PERSON (17) is deductible only from chargeable gains arising on other disposals to that same person while he is still connected.

A disposal which settles capital and income wholly or primarily for educational, cultural or recreational purposes, the beneficiaries being 'an association of persons' most of whom are *not* connected persons, is not subject to this restriction on losses.

[TCGA 1992, s 18(3)(4)].

The restriction does not apply where a person becomes absolutely entitled as against the trustee to property in a settlement (see 61.16 SETTLEMENTS).

Where the disposal is of an option to enter into a transaction with the disposer, no loss accruing to a connected person who acquires the option is allowable unless it accrues on the disposal of the option at arm's length to a person unconnected with the acquirer. [TCGA 1992, s 18(5)].

See 4.17 ANTI-AVOIDANCE for special market value provisions for disposals between connected persons.

**Debts**

A loss accruing on the disposal of a debt by a person making the disposal (the 'subsequent creditor') who acquired it from the 'original creditor' at a time when the original creditor or his personal representative or legatee was connected with the subsequent creditor, is not an allowable loss. Purchases through persons all of whom are connected with the subsequent creditor are also included as are acquisitions from the original creditor's personal representative or legatee. Where trustees of a settlement are the original creditor (or, for debts created before 6 April 2006, where the original creditor is a trustee and the debt, when created, is settled property), any loss accruing to the subsequent creditor is not allowable if he is connected with any person (or his personal representative or legatee) who becomes absolutely entitled to the debt on its ceasing to be settled property. [TCGA 1992, s 251(4)(5)].

HMRC takes the view that these provisions do not apply to debts on a security (HMRC Capital Gains Manual CG53451). For debts generally, see 25.5 EXEMPTIONS AND RELIEFS.

**Anti-avoidance**

[43.7] The following provisions apply to restrict losses in cases of avoidance.

**Arrangements to secure tax advantage**

An anti-avoidance provision applies so that a loss accruing on a disposal directly or indirectly in consequence of, or otherwise in connection with, any 'arrangements' the main purpose of which, or one of the main purposes of which, is to secure a 'tax advantage' is not an allowable loss. It does not matter whether the loss accrues at a time when there are no chargeable gains against which it could be set or whether the tax advantage would be secured for the person incurring the loss or another person.

'Arrangements' include any agreement, understanding, scheme, transaction or series of transactions, whether or not legally enforceable. 'Tax advantage' means relief or increased relief from, or repayment or increased repayment of, capital gains tax, corporation tax or income tax or the avoidance or reduction of a charge or assessment to any of those taxes or the avoidance of a possible assessment to any of those taxes.

[TCGA 1992, ss 8(2), 16A, 184D].

HMRC have published guidance on the operation of the provision. In their view, interdependence of transactions or of the terms on which transactions take place is a strong indicator (although not a necessary condition) of the existence of an arrangement. If, on the facts, any participant in arrangements is found to have a main purpose of achieving a tax advantage, that is considered to be sufficient to demonstrate that one of the main purposes of the arrangements is the securing of a tax advantage. HMRC is likely to examine carefully any relevant case in which a normal commercial objective is lacking, or where commercial objectives are not being sought in a straightforward manner. Where there is more than one way of achieving a commercial objective and a course of action is chosen on commercial grounds, any incidental tax advantage is not relevant. However, where the tax advantage was material to the choice the anti-avoidance legislation may be in point, but HMRC have indicated that this is unlikely to be the case unless there is evidence of additional, complex or costly steps included solely for tax reasons. Using a marketed tax avoidance scheme will be taken as an indicator that securing a tax advantage was a main purpose of the arrangements.

The guidance also includes 14 examples demonstrating how HMRC think the provision operates in different circumstances.

(HMRC Guidance 'Avoidance through the creation and use of capital losses', 19 July 2007).

**Miscellaneous**

Where a deemed disposal arises under *TCGA 1992, s 29(2)* on the transfer of value between different shares or rights in a company by the person controlling it, no loss is allowable on such a disposal. See 4.6 ANTI-AVOIDANCE. Value-shifting to give a tax free benefit may result in losses being allowable only to such extent as is just and reasonable. See 4.8–4.16 ANTI-AVOIDANCE.

Where there are depreciatory transactions within a group of companies or where there is 'dividend stripping' by one company holding 10% or more of a class of shares in another company, any related loss is only allowable to the extent that it is just and reasonable. See 4.22, 4.23 ANTI-AVOIDANCE.

A restriction of a loss accruing to a company which is a member of a group of companies may occur where the loss is wholly or partly referable to a time before it joined the group or the disposal of an asset which was held by another group member when that member company joined the group. See 29.20 GROUPS OF COMPANIES.

Trading losses effectively converted into allowable capital losses as in 43.21 below cannot be carried forward as a deduction against chargeable gains after the time the trade concerned ceases.

**Interaction with annual exemption**

[43.8] In giving relief for capital losses brought forward from earlier years (or carried back from a subsequent year in which the taxpayer dies — see 19.7 DEATH), such losses are deducted from the 'adjusted net gains' for the year only to the extent necessary to reduce those net gains to the amount of the annual exemption for the year, thus avoiding any wastage of losses brought forward (or back). Any balance of losses remains available to carry forward (or back). The 'adjusted net gains' are, broadly, the chargeable gains for the year less current year allowable losses. See 2.6 ANNUAL RATES AND EXEMPTIONS for the detailed definition and for worked examples. [*TCGA 1992, s 3(5)–(5C); FA 2008, Sch 2 paras 26, 56(3)*].

**Profit and losses of theatre backers (angels)**

[43.9] *Angels* are theatrical backers who invest in productions. An investment which occurs in the normal course of a backer's trade falls within the trading income or *Schedule D, Case I* rules (see Tolley's Income Tax). Special tax treatment applies to non-trading backers.

HMRC's view is that the profits of non-trading theatre angels are assessable as income whilst a loss forms an allowable loss for capital gains tax.

A 'profit' for these purposes is the return the angel receives over and above the original investment. A 'loss' arises where there is no further prospect of a return from the investment. The contract is viewed in normal circumstances as an asset for capital gains purposes (although most certainly this would have to be established on the facts of each case).

However, by concession HMRC will allow the profits and losses of non-trading theatre angels resident in the UK to be assessed and relieved accordingly under income tax rules. Where this treatment applies, any loss cannot also be treated as an allowable loss for capital gains tax purposes.

(HMRC Extra-Statutory Concession A94).

**Special reliefs for losses**

[43.10] There are a number of special rules giving rise to losses or providing for alternative reliefs and these are described at 43.11–43.19 below. See 43.1 above for a summary table.

**Assets of negligible value**

[43.11] Where the owner of an asset makes a 'negligible value' claim, he is treated as if he had sold, and immediately reacquired, the asset at the time of the claim or (subject to the following) at any earlier time specified in the claim for a consideration of an amount equal to the value specified in the claim.

An earlier time can be specified in the claim if the claimant owned the asset at that time, the asset had become of negligible value at that time and that time is not more than two years before the beginning of the tax year in which the claim is made or, for corporation tax, is on or after the first day of the earliest accounting period ending not more than two years before the time of the claim.

A negligible value claim can be made where either:

- (a) the asset has become of negligible value while owned by the claimant; or
- (b) the disposal by which the claimant acquired the asset was a no gain/no loss disposal at the time of which the asset was of negligible value and, between the time at which the asset became of negligible value and that disposal, any other disposal of the asset was a no gain/no loss disposal.

Note that (b) above applies for 2008/09 and earlier years only by concession.

For the purposes of a negligible value claim, a building may be regarded as a separate asset from the land on which it stands, but where there is a deemed sale of a building, the land comprising the site of the building (including any land occupied for purposes ancillary to the use of the building) is likewise treated as if it was sold, and immediately reacquired, at its then market value.

[*TCGA 1992, s 24(1A)–(3); SI 2009 No 730, Art 4*].

'Negligible value' is not defined but is taken by HMRC to mean 'worth next to nothing' (HMRC Capital Gains Manual CG13124).

In *Director v Inspector of Taxes* (Sp C 161), [1998] SSCD 172, a negligible value claim was refused on the grounds that the shares in question had a nil acquisition cost by virtue of *TCGA 1992, s 17* (see 44.1 MARKET VALUE) and thus could not become of negligible value (but see (b) above). See also *Barker and others v HMRC* FTT 2011, [2012] SFTD 244.

For certain qualifying corporate bonds becoming of negligible value where evidencing a 'qualifying loan', see 43.13 below.

The backdating facility above cannot be used by a company to obtain relief for a loss that would otherwise be non-allowable under the provisions for SUBSTANTIAL SHAREHOLDINGS OF COMPANIES (see 65.18).