



Entrepreneurs' Relief & The Family Business

The law as stated during this webinar is up to date as of
18th May 2017

Introduction

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Howard Hackney

Howard escaped from Grant Thornton UK LLP in 2008 where he had been a partner for over 25 years to establish his own boutique practice. During his time at Grant Thornton he was head of professional practices for the North West and head of family businesses for the UK. At Grant Thornton he had a variety of roles including office Managing Partner, North West regional marketing partner and membership of the partners appointments panel. Howard specialises in advising mid market professional practices and family businesses. In 2002 he won the CBI's national award as "Best Business Adviser".

Howard's current focus is providing "special projects" advice to family businesses with turnovers up to £30m and professional firms with up to 20 partners. His experience extends from first generation to eighth generation family businesses with all the succession issues that involves.



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Martin Dawson

Martin Dawson, director Aquarius Tax Consultancy Limited. Martin was previously a tax partner at both Baker Tilly and Grant Thornton UK LLP where he provided bespoke tax advice to owner managed businesses and high net worth individuals. Aquarius was set up in January 2010 to provide similar advice to both their own individual clients and those of smaller accounting firms that they work closely with. Aquarius have particular expertise in dealing with foreign domiciled clients (“non-doms”) and those with UK property issues.

Current projects include the restructure of several family companies (including the image right company of a well-known sportsman!), all with HMRC advanced clearance, securing significant tax savings on future value extracted. The company are also currently advising on the purchase and ownership restructure of various high value properties in London to avoid the annual ATED charge and ensure future CGT and IHT liabilities are minimised for their non-dom owners.



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Agenda

- The Fundamentals
- The shareholder
- The company
- Trusts/trustees
- Interaction with other reliefs
- Reorganisations
- Investor Relief
- Update – tax cases and Finance Act 2017
- Common Traps & Pitfalls



The Fundamentals

The Fundamentals – the shareholder

- Individuals and/or trustees only (not corporates) & £10m lifetime allowance
 - Material disposal of business assets (s.169L)
 - Business – trade, profession or vocation conducted on a commercial basis with a view to profit
 - Trade – any venture in the nature of a “trade” (as opposed to “business”)
 - No geographical restrictions (UK or overseas)
 - Disposal of whole or part of the business
 - Business asset disposal where original business sold in previous 3 years
 - “Part of a business” – no statutory definition, generally follows case law (e.g. McGregor v Adcock)
- Individual conditions
 - Officer or employee
 - Personal company – 5% threshold
 - Trading company or holding company of a trading gro
 - Relevant 12 month period



The Fundamentals – the company

- Carrying on trading activities
- Activities cannot include, to a substantial extent non-trading activities.
- HMRC view “substantial” as >20%. Need to consider “in the round”:
 - Turnover
 - Assets
 - Expenses
 - Time spent
- Areas to watch:
 - Investment property let to unconnected 3rd parties
 - Quoted shareholdings
 - Overdrawn Directors loan
 - “Excessive” cash (earmarked dividends not excessive IR Bulletin 62/2002)
- May need to consider pre-sale corporate restructure
- Furnished Holiday Lettings qualify as a trade



Trusts and trustees

Trusts & trustees

- Trustees not entitled to ER as such
- Must be a “qualifying beneficiary” (S169J(3))
- Not available to discretionary trusts, only life interest
- Beneficiary must be personally involved in ownership and conduct of the company (own more than 5%)
- No actual shareholding requirement for the trustees
- Beneficiary surrenders his ER to the trustees/joint election
- Available on share disposals or other business assets Liquidations
- Transfers in and out of trusts should qualify for holdover (s165/s260) but ER clock restarts on each transfer



Interaction with other reliefs

Interaction with other reliefs

- EIS deferral relief (Sch 5B TCGA 1992)
 - Rules changed FA 2015 (for gains after 2 December 2014)
 - Deferred 10% gains now qualify for 10% (s169U/V)
 - Election to be made by 31 January following tax year of gain
- Holdover (Gift) Relief (s.165 & s260 TCGA 1992) to individuals & trusts
 - CGT disposal created
 - ER entitlement ceases on disposal
 - ER may start again depending whether donee qualifies
- Incorporation relief (s.162 TCGA 1992)
 - Not a disposal for CGT
 - ER entitlement reset
 - Extract equity pre-incorporation



Reorganisations

Reorganisations

- “Paper for paper” transactions
 - obtain s138 Clearance (bona fide commercial)
 - generally not a disposal for CGT purposes so no ER claim
 - can make election to effectively “opt out” and treat as a disposal (s169Q)
 - loan note status impacts on tax treatment (GAAR – acceptable planning)
- Should you make the election?
 - Why? to bank ER to e.g. protect against change in rates, losing entitlement
 - “all or nothing” election
 - must make within 22 months of tax year end
 - Need sufficient cash to pay all the tax
- QCB loan notes
 - No immediate liability
 - Gross gain calculated and “frozen” until loan note redemption
 - Loss of ER as gain taxed on realisation (20% currently) - unless elect



Reorganisations/cont...

- QCB loan notes
 - can elect and “bank” ER upfront (s169R)
 - ensure sufficient cash to pay tax
 - cannot reverse election if some/all loan note becomes irrecoverable
 - no bad debt relief for CGT purposes
 - should loan notes have a bank guarantee?
 - if no guarantee, shorten length (within the 22 month election period??)
- Non QCB loan notes
 - no initial disposal due to s.135/8
 - CGT on redemption
 - Likely to be 20% (current rate)
 - Could be 10% if meet all other conditions at date of disposal
 - Can elect and “bank” ER (s169Q)
 - automatic bad debt relief (unlike QCB) but..
 - no bad debt relief if upfront election made (but capital loss to c/f)



Reorganisations/cont...

- Earn Outs
 - Marren v Ingles
 - Chose in Action – no ER on future receipts
 - Capital losses can be carried back (s279)
- EMI Share Options
 - From April 2012 ER runs from the date of grant (rather than exercise)
 - Will qualify for ER if more than 12 months from date of grant to date of sale
 - No 5% requirement – any holding will qualify



Investor Relief

Investor relief

- Introduced in FA 2016
- Qualifying gains eligible for 10%
- “Capital gains only” relief – no income tax relief like EIS
- Lifetime £10m allowance – in addition to £10m ER relief
- Conditions:
 - Must subscribe for shares (after 16 March 2016)
 - No 5% minimum shareholding
 - Trustees can qualify (s 169VC and s169VI)
 - Shares must be fully paid up in cash
 - Shares must be issued for commercial reasons (not tax avoidance)
 - Must hold shares for 3 years
 - No other connections – can hold 30% for example (unlike EIS)



Investor relief/cont....

- Cannot generally be a director or employee BUT....
 - Can become an unpaid director once IR shares have been issued (s169VM)
 - Can start “paid” employment 180 days after share issue (S169vm)
- Company must be a trading company, or the holding company of a trading group, throughout the 3 year period
- Similar “return of value” rules to EIS (other than “insignificant value”)





Update – tax cases & Finance Act 2017

Tax case update

- Susan Corbett v HMRC [2014] UKFTT
 - Employee? ER succeeded
- JK Moore v HMRC [2016]
 - Timing of director resignation and share sale important ER failed
- A Castledine v HMRC [2016]
 - Deferred shares diluting shareholding down to less than 5% ER failed
- M & E McQuillan v HMRC [2016]
 - Redeemable , non-voting shares were ordinary shares ER succeeded
- Finance Act update – no changes so non deferred



Common Traps & Pitfalls

Common Traps & Pitfalls

- April 2016 “anti-phenixing provisions”
 - Changes to TIS rules
 - Liquidations
- Company not classed as trading (see earlier slide)
 - Cash
 - Non trading activities - be careful with certain trades (e.g. caravan parks)
 - “funny” assets (yachts, racehorses, villas etc.)
- The property “hokey cokey”!
 - Do we want to retain premises
 - If owned personally & rent charged – ER restricted
- Definition of ordinary share capital and voting rights
 - Must have 5% of both
 - All the issued share capital other than capital the holders have fixed rate dividend rights but no other profit right
 - Be careful of dilution rights on exercise of share options



Common Traps & Pitfalls/cont

- Investments and trades
 - Watch where change from trade to investment
- Having the “wrong” shareholder(s)
 - Discretionary trusts
 - “wrong” family shareholdings
- Spouse shareholdings
 - H & W not aggregated
 - Must be director, officeholder or (paid) employee
 - If employee – ensure a “real” employment



Common Traps & Pitfalls/cont

- Officer or employee
 - Office – no remuneration needed
 - Employee – HMRC view is there cannot be an employment if no payment
- Watch claim deadlines
 - Must claim by first anniversary of 31 January following the tax year (s169M)
 - Be careful if Temporary Non Resident – may need to make protective claim
 - Be careful with non doms





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