

UK Tax - Investors' relief

A new relief for capital gains tax (CGT), known as investors' relief, has been introduced in the 2016 Finance Bill.

The new measure provides for a reduced 10% rate of CGT on gains accruing on the disposal of qualifying shares in an unlisted trading company, making this a very valuable relief worth up to £1 million for higher and additional rate taxpayers. The relief can only apply to the disposal of shares that were newly subscribed by an individual (other than a 'relevant employee') on or after 17 March 2016 and have been held for a period of at least three years falling after 5 April 2016.

In certain circumstances, the relief may also be available for disposals by trusts where, broadly, a beneficiary of the trust meets the conditions for relief.

An individual's qualifying gains for investors' relief are subject to a lifetime limit of £10 million. Where relief is claimed on a disposal by a trust, this reduces the £10 million limit of the beneficiary concerned.

It is therefore important for investors to plan their investments so as to maximise the benefit of this relief.

Background

The new relief was announced at the 2016 Budget with the objectives to create a strong enterprise and investment culture in the UK and ensure that

companies can access the capital they need to expand and create jobs. It also provides a financial incentive to invest in unlisted trading companies over the long term.

The Budget described the new measure as an 'extension' of entrepreneurs' relief (ER). However, although there are similarities between the reliefs, investors' relief is a new and very separate measure with some key differences. Individuals can therefore benefit from £10 million of gains taxed at the ER rate of 10% as well as a further £10 million of gains taxed at the new investors' relief rate of 10%.

Qualifying shares

Investors' relief applies to gains on the disposal of shares that are 'qualifying shares' immediately before their disposal. To be qualifying shares, the 2016 Finance Bill states that the following conditions must be met:

- The shares must be newly issued ordinary shares, having been acquired by the person making the disposal on subscription for new cash consideration. The shares must be fully paid up at the time of issue and must have been issued under a bargain for arm's length consideration.

- The shares must have been subscribed for on or after 17 March 2016 and held continuously for at least three years from April 2016 (the shareholding period). For shares issued between 17 March 2016 and 6 April 2016, this period is extended to include the time the shares were held before 6 April 2016.
- The shares must be in an unlisted trading company or unlisted holding company of a trading group when the shares were issued. Shares traded on the Alternative Investment Market (AIM) are unlisted for this purpose.
- The issuing company must be a trading company, or the holding company of the trading group, both when the shares are issued and throughout the shareholding period.
- Finally, the individual must not be a 'relevant employee' of the company. This extends to any connected persons of the individuals (i.e. spouse, civil partner, brothers, sisters, ancestors or lineal descendants). This is one of the key differences from ER, which requires the individual to be an employee or office holder of the company.

'Relevant employee'

A 'relevant employee' is any person who has been an officer or employee of the company, or of a connected company, in the period from the issue of the shares to the disposal in question, subject to two exceptions for:

- unremunerated directors who have, broadly, no previous connection with the company, nor involvement in carrying on a business carried on by the company or a connected company;
- individuals who become employees of the company or a connected company more than 180 days after the issue of the shares, provided that when the shares were issued there was no reasonable prospect of that employment being entered into, and the individual is not a director of the company or a connected company in the period concerned.

Directors are 'unremunerated' for this purpose, broadly, if they do not receive any payment other than reimbursement of expenses, dividends, commercial payments for goods, interest on loans, rent for property or payments for services provided in the course of a trade or profession (other than secretarial or managerial services, or services of a kind provided by the company or a related person to whom the services are provided).

Additional considerations

Significant government amendments have been tabled to the Finance Bill provisions, and these are taken into account above. The legislation may be amended further in the course of its progress through Parliament, but major changes now appear to be unlikely. Note also that these rules have effect for an initial five-year period.

Relief must be claimed, on or before, the first anniversary of the 31 January following the tax year in which the disposal is made.

Finally, the shares must have been issued, and subscribed for, for genuine commercial reasons and must not form part of a scheme or arrangement of which the main purposes or one of the main purposes is to avoid tax.

Planning

In view of the detailed conditions that must be met, it is essential to plan in advance to maximise the gains qualifying for investors' relief. The relief will be useful to individuals who are not employees of the issuing company and in particular, such as business angels.

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