HM Revenue & Customs

Capital gains tax: denying entrepreneurs' relief for disposals of goodwill to related companies

Who is likely to be affected?

Individuals, trustees and members of partnerships who transfer their business to a close limited company in relation to which they are a 'related party', and receive consideration in the form of cash or debt.

General description of the measure

The measure will mean that entrepreneurs' relief (ER) will not be available to reduce capital gains tax (CGT) on disposals of the reputation and customer relationships associated with a business (the 'goodwill') to a close company to which the seller is related. This change is made alongside a measure to restrict corporation tax deductions when goodwill is acquired from a related party on incorporation.

Policy objective

The measure removes an unfair advantage available to proprietors of businesses who sell their business to a close company to which they are related in order to extract funds from the business at a special, low, rate of CGT rather than the normal rates of income tax and national insurance contributions.

Background to the measure

The measure was announced at Autumn Statement 2014.

Detailed proposal

Operative date

The measure will apply to disposals of goodwill to a related close company on or after 3 December 2014.

Current law

The ER provisions are at sections 169H – 169S Taxation of Chargeable Gains Act 1992 (TCGA). ER reduces the rate of CGT on the disposal of all or part of a business to 10 per cent, from the normal 18 per cent or 28 per cent. Gains and losses on relevant business assets (defined at section 169L) are combined and the net gain taxed at the reduced rate.

Proposed revisions

Legislation will be introduced in Finance Bill 2015 to amend TCGA in order to exclude goodwill from the definition of 'relevant business assets' at section 169L TCGA, so that gains on disposals of goodwill to a close company by an individual who is a related party (under the definition at section 835 Corporation Tax Act 2009) will be charged at the normal rates of CGT (subject to other reliefs).

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2014-15</td><td>2015-16</td><td>2016-17</td><td>2017-18</td><td>2018-19</td><td>2019-20</td></tr>
<tr><td>+5</td><td>+30</td><td>+80</td><td>+110</td><td>+135</td><td>+155</td></tr>
<tr><td colspan="6">These figures are set out in Table 2.1 of Autumn Statement 2014, as part of Self-incorporation: intangible assets, and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside Autumn Statement 2014.</td></tr>
<tr><td>Economic impact</td><td colspan="6">The measure is not expected to have any significant economic impacts.</td></tr>
<tr><td>Impact on individuals, households and families</td><td colspan="6">Individuals (including partners) who transfer their businesses to a company which they control in order to claim ER on the gains accruing will be most affected, though this will not necessarily result in a CGT charge in all cases.

No impact on families or households because this measure affects individual business owners and partners, and only in those capacities.</td></tr>
<tr><td>Equalities impacts</td><td colspan="6">The measure is not expected to have a significant impact on those with legally protected characteristics. Those affected will broadly reflect the composition of ER claimants.</td></tr>
<tr><td>Impact on business including civil society organisations</td><td colspan="6">This measure is expected to have a negligible impact on businesses. The direct impact will be on individuals when they incorporate their business on the specified terms, rather than on the businesses itself or on incorporations generally. Capital gains tax incorporation relief remains available, subject to the relevant conditions being met, and where it is due there will be no CGT charge on the incorporation of a business.

This measure is expected to have no impact on charities. Charities are exempt from tax on gains applied for charitable purposes.</td></tr>
<tr><td>Operational impact (£m) (HMRC or other)</td><td colspan="6">The additional costs and savings for HM Revenue and Customs in implementing this change are anticipated to be negligible.</td></tr>
<tr><td>Other impacts</td><td colspan="6"><u>Small and micro business assessment</u>: small and micro businesses which are carried on by individuals, alone or in partnership, can benefit from being transferred to a company under the same ownership. This measure does not obstruct such incorporations, for which tax relief remains available to the former proprietor.

Other impacts have been considered and none have been identified.</td></tr>
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Monitoring and evaluation

The measure will be monitored through monitoring of disclosures of new avoidance schemes to circumvent the measure, and through regular communication with taxpayers and practitioners affected by the measure.

Further advice

If you have any questions about this change, please contact Rob Clay on 03000 570649 (email: rob.clay@hmrc.gsi.gov.uk).

Declaration

David Gauke MP, Financial Secretary to the Treasury, has read this Tax Information and Impact Note and is satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impacts of the measure.