

# New challenge to entrepreneurs' relief

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HMRC has found a new excuse to deny entrepreneurs' relief to shareholders who sell their shares back to the company.

here is now a huge difference between the rates of CGT (10% and 20%) and the higher rates of income tax (40% and 45%). This encourages company owners to extract value from their companies a form which is subject to CGT.

## Purchase of own shares

When a shareholder sells their shares back to their company, under a purchase of own shares (POS) arrangement, the proceeds are taxed as income. However, capital gain tax treatment for those proceeds can be achieved if the following conditions are all met:

- seller has held the shares for at least five years
- seller is UK resident
- the purchase is for the benefit of the trade
- company is unquoted
- the company is trading or holding company of a trading group
- seller's shareholding (including associates' holdings) are substantially reduced or eliminated by the purchase; and
- seller and his associates are not connected with the company immediately after the purchase.

The company must apply to HMRC in advance of the POS for clearance that the proceeds will be subject to CGT rather than income tax.

## Payment dates

If the company has the cash available to pay the shareholder the full amount agreed for his shares, the POS can proceed without further complications.

Where the company can't pay the full sales value at the date the sale is due to complete, it may need to pay the amount agreed in tranches over a number of years. For a payment by tranches arrangement to be given clearance as a capital distribution, the contract for the acquisition of the shares must contain multiple completion dates which align with the dates on which the proceeds are paid.

## How tranches work

The shares are sold back to the company on day one. This is the exchange date for the whole contract and also first completion date. It is on this date that the shareholder

loses beneficial interest in all his shares. If the shareholder is a director this is the date on which he should resign as a director.