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Monday 12 October 2020

To whom it may concern,

**Capital Gains Tax review – Main Call for Evidence**

We welcome the opportunity to respond to your Capital Gains Tax (CGT) Main Call for Evidence.

The Quoted Companies Alliance *Tax Expert Group and Share Schemes Expert Group* has examined the proposals and advised on this response from the viewpoint of small and mid-size quoted companies. A list of Expert Group members can be found in Appendix A.

If you would like to discuss our response in more detail, we would be happy to attend a meeting.

Yours sincerely,

A handwritten signature in blue ink, appearing to read "T. Ward".

Tim Ward  
Chief Executive

## **Structural CGT issues**

### **Acquisition and disposal**

#### **Q1 Is the scope and boundary of CGT clear? Is it always obvious when an event is chargeable?**

On balance, we do not believe that the general public are aware of when and how CGT is due. Without intervention and advice, most taxpayers would not be aware of a liability following a transaction. Taxpayers are not aware of the pay and file requirements for the sale of residential properties, for example. The tax tribunal's rulings against taxpayers who are unaware of the provisions is also evidence of a lack of information in the public domain.

One of the contributory factors to this lack of awareness is the lack of media attention. Whilst there is a lot of media attention on self-assessment, there is little on CGT. Increasing the coverage of CGT through broadcast, print and social media would help enhance awareness considerably.

The timing of a chargeable event can also be misunderstood as acquisition and disposal arise at the time of the contract not necessarily at the completion of the transaction or when the consideration is paid. Without professional advice, this might not be clear.

There may be an opportunity for innovations in digital taxation to raise awareness for taxpayers. HMRC's Making Tax Digital (MTD) systems should be made capable of raising notifications about the status of declared transactions and provide direction for where further information can be found.

#### **Q2 How generally aware are taxpayers of their (potential) CGT liabilities following a disposal? Could/should they be made more aware, and if so how?**

In general, taxpayers who regularly buy and sell assets will have advisers to indicate and calculate potential CGT liabilities. However, other taxpayers will have to seek this information for themselves, which is not always easily found or understood. An example of where taxpayers are not aware of their potential CGT liabilities following a disposal is gift property relief.

In order for taxpayers to be made more aware, it should be incumbent on solicitors, estate agents, banks, and financial houses to indicate the necessity for self-assessment filing so taxpayers are not left unaware.

#### **Q3 To what extent do the current CGT rules influence decisions around whether, how or when taxpayers acquire or dispose of assets? And to what extent and how do taxpayers adjust their activity to reflect this?**

Regarding the extent to which the current CGT rules influence decisions, when there is an anticipated change of rate, taxpayers will accelerate or delay disposals. Taxpayers will often make disposals to crystallise a gain that is less than the annual exemption so that no tax is paid. Similarly, taxpayers will wait until losses are available until more significant disposals are made.

#### **Q4 Are there any specific practical challenges for taxpayers in dealing with the CGT aspects of acquiring and disposing of assets?**

In respect of the practical challenges for taxpayers in dealing with the CGT aspects of acquiring and disposing of assets, issues commonly arise around spousal transfers, trading vs non-trading, the

complexities in legislation surrounding main residence relief, gift relief, and Business Asset Disposal Relief. These issues typically arise where the legislation is more complex and where matters are less clear-cut.

See also the point about the timing of the disposal mentioned in Q1.

**Q5 Is it always clear and easy to understand which expenses (including capital improvement, acquisition or disposal expenses) qualify for CGT purposes? Are the rules on qualifying enhancement expenditure clear and reasonably straightforward to operate in practice?**

No – it is not always clear and easy to understand which expenses qualify for CGT purposes. It is often the case that taxpayers are not aware of, or confused by, what can be deducted as capital, what qualifies for capital allowances, what is a revenue deduction for income tax, and what cannot receive any relief. The finance costs are a significant area in which taxpayers are confused, as a result of some being allowable and others not.

In order to ameliorate these issues, additional clarity needs to be provided, such as through the provision of clear guidance on specific expenditure. This could be enshrined in legislation or included within the HMRC manuals.

**Q6 Are there particular practical challenges or issues arising from the CGT rules about acquiring, disposing of or transferring assets on marriage (or civil partnership), separation or divorce?**

Yes – there are practical challenges and issues that arise from the CGT rules about acquiring, disposing of or transferring assets on marriage (or civil partnership), separation or divorce. These are due, in part, to the complexities and inconsistencies that exist within the rules. One of the chief issues that exists is the incorrect assumption that spousal exemptions subsist until divorce, as they do for Inheritance Tax. There is also a practical challenge as CGT often needs to be paid during the period of separation and on any divorce settlement. The liabilities tend to be determined at the point of divorce, whereas, after death, there is more time to determine IHT liabilities.

**Q7 Are there particular issues around the boundary with income tax e.g. shares or share rights received by employees or the boundary between trading and investment?**

We have no comments on the boundaries between trading and investment.

There remains a common misunderstanding by individuals about the tax treatment of shares acquired for market value by founders or other employees who think they are making a capital investment. These individuals often fail to appreciate the shares will be employment related securities.

### **Annual exempt amount (AEA)**

**Q8 In your experience, to what extent do individuals or their agents arrange to time disposals of assets in such a way as to maximise use of their AEA to manage down their tax liabilities?**

The QCA's members indicated that individuals or their agents, arrange the timing of disposals of assets to maximise use of their AEA. They do so to manage down their tax liabilities to the fullest extent. Individuals, or their agents, will specifically time and tailor their disposals to optimise the use of the AEA.

**Q9 Could there be a simpler or more targeted way of taking small gains out of tax?**

Yes – we believe that the removal of the test for declaration at proceeds exceeding four times the AEA and stating that gains below the AEA need not be declared, is a simpler way of taking small gains out of tax.

### **Different rates of CGT (10%/20%/18%/28%)**

**Q10 To what extent do the different rate of CGT cause complexity? Is it always clear which tax rate should apply? Which situations present specific problems? Does the dependence on the income tax higher rate threshold make this inevitable? Do you think the rates position can be made simpler, and if so how?**

We believe that the different rates of CGT are not straightforward and increase complexity. Furthermore, the different rates often mean that additional work and expense is often required to apportion valuation from the disposal of different types of assets.

Whilst a flat rate may be beneficial, issuing alternatives may only serve to create further complexities.

### **Issues commonly affecting individual taxpayers**

#### **Reliefs and exemptions**

##### **Principle Private Residence Relief (PPR)**

**Q11 Are you aware of situations where the current rules are not easy to operate perhaps because of changes in society or patterns of work (such as home-working, taking in a lodger, letting out a bedroom to tourists, or the use of gardens or grounds)?**

We have no comments.

**Q12 Are the ancillary reliefs and occupation rules consistent with what you consider PPR is aiming to achieve? If not, what would make them simpler to apply or better achieve these aims?**

We have no comments.

**Q13 How do you find the principle and practice of making a nomination? Are there better ways of achieving the same ends?**

We have no comments.

#### **Chattels exemption**

**Q14 Are there any aspects of the taxation of gains arising from the disposal of chattels that you consider would benefit from being simplified?**

Almost all of the chattels rules would benefit from simplification. The rules are seldom used and too complex. The only exception is the £6,000 minimum proceeds rule.

**Q15 Is it clear to taxpayers that gains on significant chattels are potentially taxable? Or is there a general lack of awareness?**

There is a significant lack of awareness that gains on chattels are potentially taxable. Members of the QCA have indicated their awareness of cases where the taxpayer has sold something and been completely unaware of the tax implications.

### **Issues commonly affecting business owners and investors**

#### **Business lifecycle**

**Q16 Are there features of CGT that present barriers or distortions at any of these stages? Are the rules simple to understand and apply correctly? Please provide examples along with any suggestions on how the rules could be made simpler.**

Regarding Business Asset Disposal Relief (BADR), we believe that this relief can be simplified. Given the positive role of this relief and its particular importance for employees, the QCA would suggest the removal of the complex 5% holding requirements for employees. The holding requirements lead to unfair treatment if new investments or option exercises cause dilution or restructuring to enable the relief to continue. A simplification of this condition would better support employees seeking to participate in the growth of their business.

We also believe that the alignment of the BADR rules with those of Business Relief would help to increase the simplification of the rules.

**Q17 Do you know of occasions when CGT rules have affected business decision making more generally, including decisions regarding the structure of a business or the choice of business vehicle (for example a corporate entity, partnership, unincorporated business)?**

Yes – it is commonplace for CGT rules to affect business decision-making, including decisions regarding the structure of the business. For instance, many smaller companies are set up so that the owners of the company will receive BADR upon the sale of the company. Additionally, deals are also often timed and structured in a way that allows this with directorships being added so that they are able to claim the relief in the future. Finally, if assets are likely to affect the eligibility, it is often the case that these are placed into standalone companies.

As a result, the rules relating to CGT can be considered a major area in planning the structure of a business.

**Q18 Please tell us about any complications or rules which unduly affect the way businesses operate if payment for the sale of a business is not made in cash but in some other way (such as qualifying and non-qualifying corporate bonds, deferred consideration and earn outs). To what extent is there a business tension between claiming a tax relief at the point of sale as opposed to deferring the tax charge until cash is received?**

There are instances where complications arise which affect the way businesses operate.

For example, if a deal is made that leaves the vendors with less than 5% of the share capital and no continuing employment, there is pressure on both the vendor and the purchaser to make the deal suitable for an election to treat the proceeds as received immediately in order to claim the relief. This demonstrates that a deal has been skewed in order to suit the desired tax outcome.

Furthermore, when deferred consideration on a share sale consists of shares or non-QCB loan notes, the gain arising on the disposal of the earn out right rolls over into the shares or the loan notes and the tax point is deferred until the shares or loan notes are disposed of. However, if the deferred consideration is in the form of QCB loan notes the gain that would have arisen is frozen and is charged to tax when the loan notes are disposed of. In both cases, this is subject to the ability of the individual to elect to trigger a disposal for the purposes of claiming BADR.

The QCB/non-QCB distinction is unnecessarily complicated and rarely understood by taxpayers. This is partly a consequence of the nomenclature, but it is also a result of the definition in s117 TCGA which means that often the only difference between a QCB and a non-QCB is the inclusion of a right of conversion into a foreign currency.

In order to correct this complication, it should be possible to remove the distinction and have a simpler mechanism whereby an individual who receives loan notes as consideration on a share sale is subject to rollover, subject to the ability to elect to freeze the gain or crystallise the gain.

Finally, the tax treatment of earn-outs can be uncertain. Although HMRC has flagged certain indicators in the employment related securities manual, it is often difficult to apply the indicators and different advisers take different views. It appears that earn-out terms are evolving (for example, longer earn-out periods and a requirement to remain in the business for longer due to increased uncertainty) which creates additional uncertainty as 'market practice' is no longer so consistent. While we appreciate that this may not be an easy fix, additional clarity around the conditions for capital gains treatment would be helpful. Failing that, a procedure to allow clearance or assurance would clarify the tax status of earn-outs ensuring tax is correctly paid and reducing the uncertainty that can hold up the completion of transactions. It is worth noting that earnouts or other deferred consideration are commonplace in commercial transaction.

### **Reliefs available to business owners/shareholders**

**Q19 Is the scope of each of these reliefs intuitive or are there unexpected differences between them that create practical problems for businesses? Are there aspects of any of these reliefs that you consider are unclear or particularly difficult to utilise in practice?**

The tax rules surrounding corporate bonds and the CGT legislation relating to bonds in general are difficult and too complex for the layman taxpayer to interpret and navigate. This is outside of the complexities of the Transactions in Securities provisions which require HMRC clearances to ensure that business sellers are not subject to Income Tax on what are intended to be capital proceeds.

**Q20 Are there aspects of these reliefs which distort business decision making (for example in respect of such areas as the timing of the disposal of an asset, or how much cash to accumulate on a company balance sheet) or are inconsistent with your understanding of what the relief is aiming to achieve? Are there any ways in which they could be made less distortive?**

Please see our response to Q17 above.

**Q21 Should gift relief be extended to cover a greater range of business and investment assets as it was until 1989? What would the effect of this be? And would any extension open up unintended avoidance opportunities?**

Yes – we believe that gift relief is unduly restrictive and should apply to a greater range of business and investment assets. As part of this, we believe that gift relief should be extended to all assets passed through the familial line. CGT will still eventually be paid on the sale of the asset as the chain of the relief is unlikely to be unlimited. More gifts will occur in families and there will be limited effect on the Exchequer's tax take.

### Specific asset classes

**Q22 Are there any aspects of the rules relating to the taxation of gains or losses realised on the disposal of shares and securities that are particularly complex to understand or apply? Are you aware of any difficulties in ascertaining the base cost of such assets, such as the share matching rules?**

On balance, we believe that the rules relating to the taxation of gains or losses realised on the disposal of shares and securities are not particularly complex to understand or apply. The changes to the rules implemented over the years have simplified them, and, as a result, there are few issues that arise in practice.

That said, the matching rules do add complexity. One way in which this complexity can be reduced would be to extend the rules that say taxpayers can match an acquisition and disposal on the same day. For income tax purposes, HMRC guidance says taxpayers can use the actual selling price where the sale takes place on the day of acquisition or the next 2 dealing days. This recognises that on a large vest it can take a broker a few days to action a sell to cover. If the CGT rules matched an acquisition and disposal on the same day, or in the few days following the acquisition, this could be easier.

Furthermore, the rules for determining the CGT base cost are a prime target for simplification. Currently, different rules apply depending on whether a share acquisition is taxed under the securities option rules or as general earnings. Commercially, very similar arrangements can be taxed under different rules, for instance, RSU can require close analysis to determine which set of rules apply. This has a particular impact on internationally mobile employees. If the general earnings rules apply, s17 gives a market value base cost. If the securities option rules apply, s144ZA disapplies s17, but s119A(3)(d) uplifts the CGT base cost by reference to income arising on vest/exercise. Where the employee has only been in the UK for part of the vesting period they will only pay income tax on part of the vesting/exercise, thus meaning an immediate gain if the shares are acquired under an RSU, taxed as a securities option, and then sold as they will not have the full base cost.

For restricted shares, s149AA determines the base cost by reference to the amount paid for the shares and the amount treated as general earnings. However, amounts that would have been exempt earnings for UK purposes are excluded. Under UK rules, if restricted shares are subject to a risk of forfeiture not capable of lasting more than 5 years, the amount that would have been taxed as general earnings on acquisition is exempt (as the UK restricted securities rules and imposed a tax point on vest instead). This means someone outside the UK who acquires shares with a risk of forfeiture has no CGT base cost, which is an issue if they come to the UK and want to sell the shares. For CGT purposes, there is no credit for any foreign tax paid on acquisition. Any deductions would have to be addressed via FTC relief, which can be complex.

Though the value of some employment-related securities can be significant, many employees will be awarded small numbers of shares, often on an annual basis. This means the application of the matching

rules might create time consuming complexities for the employee and HMRC in checking calculations without providing tax revenue.

Prescribing that all shares acquired under an employee share plan have a base cost, which reflects the market value of the share at the acquisition date, whether or not the individual was in the UK at acquisition, would greatly simplify the system.

**Q23 Are there any aspects of the taxation of gains arising from the disposal of investment properties, leases, land or buildings that you feel would benefit from being simplified?**

Yes – we believe that more prescriptive legislation and guidance is required in order to help determine what is deductible in a capital gains tax computation.

**Q24 Are there other asset classes (such as for example crypto assets) which present challenges or complexity for individuals on disposal?**

In a similar vein to our answer to Q23 above, more legislation and guidance is required for the disposal of crypto assets. While these assets are still relatively rare, there is little understanding of the tax consequences even amongst the advisory community.

#### **Company issues**

**Q25 Are there particular areas of complexity that relate exclusively to companies? And if so, should these be simplified or made more consistent?**

Yes – there are areas of complexity that relate exclusively to companies. For instance, while the removal of indexation from the end of 2017 assisted in a streamlining of the rules for companies, the computation of that indexation for assets up to that date does make for added complications.

Furthermore, the single rate is helpful, but the use of losses from capital disposals and the use of other losses against gains needs to be amended in order to increase consistency and aid compliance.

#### **Administration of CGT (for individuals, investors and unincorporated businesses)**

##### **Administration**

**Q26 Please describe any problems you have had (or anticipate having) in navigating the online systems or forms and provide any suggestions you have on how the forms or related guidance could usefully be simplified, made clearer or made easier to complete. Please specify which method(s) of reporting your experience relates to.**

We have no comments.

**Q27 Do you have any suggestions about how HMRC could use information it currently has or has access to, in order to reduce administrative burdens, improve customer experience and ensure compliance in respect of individuals' and businesses' CGT obligations? Does HMRC get the balance right between asking for information to avoid unnecessary enquiries and streamlining the experience for those with simple affairs?**

We have no comments.



## Payments

**Q28** Please comment on any complexities or practical problems that you have experienced (or anticipate) in relation to the process of paying CGT. Please specify which reporting system(s) your payment(s) relate to.

Our members have indicated that they are not aware of any complexities or practical problems with CGT payments.

## Claims

**Q29** Are you aware of any particular practical or technical issues (relating to for example record keeping, awareness, use of ringfencing rules, timing deadlines or other challenges) for losses, other claims, or clearances that you feel should be highlighted as part of this CGT review?

We note, employee shareholders with minor shareholders, may be unaware of their record keeping requirements and reporting obligations.

## Record keeping, valuation and calculation of any tax payable

**Q30** What, if anything, could be done to help taxpayers to more easily fulfil their record keeping obligations and calculate any tax payable in relation to their capital gains?

We have no comments.

**Q31** Have you encountered any difficulty with valuing assets either at acquisition or disposal? What, if anything, could HMRC do to simplify the valuation requirements or processes without opening up unintended avoidance opportunities?

In order to improve the process of valuing assets at either acquisition or disposal, HMRC could allow a professional valuation from an approved surveyor, or other professional, when provided with the tax return. This would remove the need for HMRC to assess the valuation and make the process more timely and efficient.

A select few valuations could still be checked through the enquiry process.

Having said that, on the whole, HMRC's Shares and Asset Valuation team is generally able to process valuations efficiently.

**Q32** Would changing to a more recent rebasing date than 1982 make finding the base cost of a disposal easier or would any such benefit be outweighed by an increase in the number of valuations that would then be required?

We have no comments.

## Estates in administration

**Q33** Are there particular aspects of the taxation of capital gains made by those administering an estate that could be simplified?

We have no comments.

**Interaction between CGT and IHT and with other taxes**

**Q34 To what extent does the absence of a CGT charge on death and transferring those assets at market value on death distort and complicate the decision-making process around passing on assets to the next generation?**

We believe that the absence of a CGT charge on death and transferring those assets at market value on death greatly distorts the decision-making process.

**Q35 Are there any aspects of the taxation of gifts or other disposals that are not made at market value, that you feel would benefit from being simplified? Should the range of assets eligible for a tax deferral when they are gifted be broadened to include a greater range of assets? And would any extension open up unintended avoidance opportunities?**

We have no comments.

**Q36 Are there instances where you feel the interaction of CGT with other areas of tax results in particular complexity or difficulty in applying the rules correctly? Are there definitions within CGT that would benefit from closer alignment with the definitions found in other taxes? Please provide examples, as well as any suggestions for ways to simplify the system.**

We have no comments.

**Q37 Are there instances where you feel the interaction of CGT and capital allowances (in respect to income or corporation tax) results in particular complexity, difficulty in applying the rules correctly, or unexpected tax outcomes?**

Yes – there are instances where the interaction of CGT and capital allowance results in difficulties. Regarding commercial properties, for example, there is refurbishment expenditure that is not deductible as revenue or in a capital gains computation or for capital allowances. This expenditure needs an outlet as it would seem unfair that some refurbishment expenses are overlooked unless the costs increase the proceeds from granting the lease.

**Other areas of complexity**

**Q38 Are there any particular areas of complexity that are unique to partnerships?**

Yes – the transfer of assets between partners is particularly complex. For instance, when assets are reapportioned on the admission and retirement of partners, capital disposals are crystallised, this has obvious CGT implications.

**Q39 Please tell us about any other areas of complexity not covered above in applying any CGT reliefs, thresholds, or administration not already mentioned in your response, along with any suggested improvements to the CGT rules or legislation.**

There is a relief for bringing an asset into stock, but not for taking stock into assets. It would be more appropriate if there was a relief in both directions.

**Q40 Are there any areas of complexity that are specific to England, Scotland, Wales or Northern Ireland?**

We have no comments.

#### **Wider CGT framework**

**Q41 Do you think that there are ways in which the taxation of capital gains should be reformed more widely to simplify the regime for the benefit of taxpayers? If so, how?**

Please refer to our submission in response to the first section of the call for evidence (available [here](#)).

**Q42 Do you think it would be reasonable for some reliefs or exemptions to be removed if they fail to meet what you regard as their policy objective or are infrequently used? If so, which ones?**

We consider that rollover relief could be removed as it is very rarely used, as it covers very few assets and assets that are esoteric in nature.

**Q43 Are there any useful lessons that can be learned from the UK's historic CGT regime or other countries that would be relevant to the UK today? If so what, and from which countries?**

As indicated in our response to the first section of the call for evidence, some of our members have considered a similar approach to the US, where gains on assets held for less than a year are reclassified as income. This rule would be much simpler. A return to a single headline rate that tapers over time is perhaps a simpler concept than the multitude of different rates and circumstances and rules that we now have. A return to a system that split business (lower tax rate) and non-business (higher tax rate) assets and a tapering rate to further reduce tax charge for longer asset holding could be welcome with shares acquired under an employee share scheme falling to being charged as business assets.

## **Appendix A**

### **The Quoted Companies Alliance Tax Expert Group Expert Group**

Paul Fay (Chair)	Crowe UK LLP
Mark Allwood	Haysmacintyre
Paul Attridge	Bright Grahame Murray LLP
Emma Bailey	Fox Williams LLP
David Blumenthal	Clyde & Co LLP
Edward Brown	Grant Thornton UK LLP
Tom Gareze	PKF Littlejohn LLP
Rachel Gauke	LexisNexis
Oliver Gutman	Shakespeare Martineau LLP
Yuri Hamano	BDO LLP
Daniel Hawthorne	Dechert
Hannah Jones	Deloitte LLP
Mark Joscelyne	CMS
Sabina Marguiles	LexisNexis
Zoe Peck	Mazars LLP
Dan Robertson	RSM
Matthew Rowbotham	Lewis Silkin
Ray Smith	Clyde & Co LLP
Andrew Snowdon	UHY Hacker Young
Peter Vertannes	KPMG LLP
Paul White	Druces LLP

### **The Quoted Companies Alliance Share Schemes Expert Group Expert Group**

Fiona Bell (Chair)	RSM
Tristan Adams	Link Asset Services
Barbara Allen	Stephenson Harwood
Emma Bailey	Fox Williams LLP
Dave Bareham	Smith & Williamson LLP
David Baxter	Stephenson Harwood
Danny Blum	Eversheds Sutherland
Ian Brown	Slaughter & May
Michael Carter	Osborne Clarke
Sara Cohen	Lewis Silkin
Stephen Diosi	Mishcon De Reya
Suzy Giele	Lexis Nexis
Andy Goodman	BDO LLP
Ellisavet Grout	Travers Smith LLP
Juliet Halfhead	Deloitte LLP
Caroline Harwood	Crowe UK LLP

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Lea Helman	Lexis Nexis
Stuart James	MM&K Limited
Liz Hunter	KPMG
Graham Muir	CMS
Isabel Pooley	Grant Thornton UK LLP
Jennifer Rudman	Prism Cossec
Richard Sharman	FIT Remuneration Consultants