HM TREASURY

HM Revenue & Customs

Simplification review:

capital gains rules for groups of companies – a consultation document

February 2010

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Basic information

Subject of this consultation:	The proposals in this consultation document are aimed at simplifying the legislation on capital gains for groups of companies.
Scope of this consultation:	This consultation deals with the simplification of legislation on capital losses after a change in ownership, legislation on value shifting and depreciatory transactions, and legislation on degrouping.
Impact Assessment:	The Impact Assessment for the proposals set out in this consultation document can be found at: http://www.hm-treasury.gov.uk/consult_simplification_capitalgains.htm
Who should read this:	The Government would like to hear the views of business, as well as the views of representative bodies and tax advisers, on the proposals set out in this consultation document.
Duration:	The consultation period for this document runs from 22 February 2010 to 17 May 2010.
Responses and enquiries:	Responses and enquiries should be sent to: The Related Companies Simplification Review Team Room 2/E1 HM Treasury 1 Horse Guards Road London, SW1A 2HQ Alternatively, please email: relatedcompanies.simplification@hmtreasury.gsi.gov.uk Telephone enquiries: 020 7270 6104
Additional ways to become involved:	The Government intends to hold a workshop to discuss stakeholder views on the simplification proposals, before the end of the 12 week consultation period. Please send your expressions of interest to the e-mail address above and indicate your preferred dates by Friday 12 March.
After the consultation:	The answers the Government receives to the questions on the proposals will assist in the development of any package of reform, with a view to legislating at the earliest practical opportunity.
Getting to this stage:	Since initiating an online survey on the corporation tax rules for related companies at the 2007 Pre-Budget Report, the Government held initial discussions with business to identify specific rules within the capital gains legislation (as it applies to groups) that would benefit most from simplification, and to develop workable proposals for simplifying these rules. The Government then published a discussion document containing a number of options for simplification, in July 2009. The proposals in this consultation document have been informed by the helpful written responses received to the discussion document and by a stakeholder workshop held in September 2009.

Contents

1 Introduction

1.1 In the 2007 Pre-Budget Report, the Government renewed its commitment to tax simplification, launching three reviews to evaluate how a range of tax legislation could be simplified. The simplification reviews cover VAT, anti-avoidance legislation and the corporation tax (CT) rules for related companies. This consultation document arises out of the related companies simplification review.

1.2 This document develops the simplification options outlined in the discussion document published by HM Treasury and HM Revenue and Customs (HMRC) in June 2009.[1] The proposals set out in Chapters 2 to 4 below build on further work undertaken by the Government and on the constructive input provided by stakeholders in response to the discussion document.

Related companies simplification review

1.3 At the 2007 Pre-Budget Report, the Government initiated an online survey on the CT rules for related companies, to identify which areas of those rules were leading candidates for simplification. The responses received to this survey identified two immediate priorities for simplification: the associated companies rules as they apply to the small companies' rate of CT, and the capital gains rules as they apply to groups of companies. This consultation document concerns the capital gains rules for groups.

1.4 During 2008 and the first half of 2009, the Government held a series of productive informal discussions with business representatives. The aim of these initial discussions was to identify specific rules within the capital gains legislation (as it applies to groups) that would benefit most from simplification, and to develop workable proposals for simplifying these rules.

1.5 One area of the capital gains legislation identified by business as a priority for simplification was the rule on notional transfers within a group of companies. At Budget 2009, the Government announced that it would simplify this legislation, and the measure was subsequently legislated in Finance Act 2009.[2] The measure was widely welcomed by business as a helpful simplification.

1.6 Following the dialogue with business, the Government published a discussion document in July 2009 outlining various options for simplifying three other areas of the capital gains legislation for groups. These related to:

- Capital losses after a change in ownership
- Value shifting and depreciatory transactions
- Degrouping charges

[1] *Simplification review: capital gains rules for groups of companies – a discussion document.*

[2] Clause 31, Finance Act 2009

Policy context

1.7 While there is necessary complexity within the capital gains rules for groups of companies, the Government believes that there is scope for simplification, either by clarifying the existing rules, by improving their design, or by repealing parts of the legislation that have been superseded. In addition to aiming to simplify legislation, the Government has also made clear from the outset of the related companies simplification review that it regards the matching of tax outcomes with economic outcomes for groups of companies as another goal. This helps ensure fair tax treatment between taxpayers and reduces any distortion to commercial decision-making.

1.8 As far as possible, the capital gains rules for groups of companies are intended to recognise that a group of companies operates as a single economic entity. This principle underpins the 'no-gain-no-loss' asset transfer rule,[3] which allows companies within the same corporate group to transfer assets between one another on a tax-neutral basis.

1.9 A consequence of the 'no-gain-no-loss" rule is that value can be moved between companies in a group such that when a company is sold by the group, the tax gain or loss on the shares may not reflect the economic gain or loss on the assets during the time they were owned by the group. This effect may be increased by the ability to subscribe for further share capital in a group company, so increasing its capital gains base cost.

1.10 The capital gains regime for companies contains a number of provisions designed to align tax outcomes with the economic gains or losses on assets that have arisen during the time the assets are owned by a particular group. The value shifting and depreciatory transactions rules and the degrouping charges rules, which the Government proposes to simplify, are examples of such provisions.

1.11 Any reforms arising from the simplification review will be consistent with the requirement that the underlying policy and anti-avoidance functions of the existing regime are to be preserved.

Summary of proposals

1.12 The July 2009 discussion document included options to simplify the capital gains rules for groups in the following areas:

- **Capital losses following a change in ownership.** In December 2005, the Government introduced three Targeted Anti-Avoidance Rules (TAARs). The second TAAR was aimed at preventing 'capital loss buying', i.e. the practice of acquiring a company primarily for the purpose of gaining access to its capital losses, whether these are realised or latent. The discussion document contained four options for simplifying some of the legislation pre-dating the TAARs that governs the use of capital losses after a change in company ownership.
- **Value shifting and depreciatory transactions.** The value-shifting rules have been identified as particularly complex, and therefore a priority for simplification. The discussion document identified two leading alternative possibilities for simplifying these rules, along with the separate option of introducing a time limit for the operation of the rule on depreciatory transactions.

[3] Section 171, Taxation of Chargeable Gains Act 1992

- **Degrouping charges.** The degrouping charge ensures that if a company leaves a group, holding an asset acquired through a tax-free transfer from a fellow group member within the last six years, then any gain or loss deferred at the time of the transfer is reinstated. However, the Government acknowledges that in some circumstances the current rules can sometimes lead to economic double taxation. The discussion document contained six options for simplifying the degrouping charge rules, along with a further option to simplify the interaction between the degrouping charge and the Substantial Shareholdings Exemption (SSE).

1.13 This consultation document puts forward detailed proposals – including draft legislation – in each of these three areas. The proposals have been informed by the helpful written responses received to the discussion document and by a stakeholder workshop held in September 2009. A summary of the written responses to the discussion document is provided at Annex A.

1.14 Chapter 2 of this consultation document sets out the Government's proposals to simplify the rules governing the use of capital losses following a change in company ownership in cases where the targeted anti-avoidance rules on gain and loss buying do not apply. The main proposal is to remove restrictions on the use of losses that are not realised at the time a change in ownership takes place. As a result, there will no longer be any requirement to apportion gains and losses on pre-entry assets, and many of the complex rules applying to holdings of shares and securities can be repealed. An additional proposal is for the amended rules to apply in a similar way to assets used for the purposes of trades and other businesses, rather than being limited to trades alone.

1.15 Chapter 3 sets out the Government's proposals to simplify the legislation in respect of value shifting and depreciatory transactions. The main elements of the Government's proposals are to replace the complex value shifting rules applying to groups at sections 31-34, Taxation of Chargeable Gains Act 1992 (TCGA) with a simpler, motive-based rule. In addition, the Government proposes to introduce a time limit of 6 years to the depreciatory transactions rules at section 176 TCGA.

1.16 Chapter 4 contains the Government's proposals to simplify the degrouping charge rules and to ensure a closer matching between economic outcomes and tax outcomes. The Government's proposals include several elements, one of which is to clarify the existing exception to the degrouping charges for asset transfers between "associated companies" that leave a group together. The Government also proposes to ensure any degrouping charge on trade assets can come within the exemption where the SSE applies, including changes to the SSE rules which will make it easier for groups to reorganize their trading assets prior to a disposal while still benefiting from the exemption. A further element of the proposals is to ensure the degrouping charge is generally payable by the vendor group rather than the company which has been sold. In addition, the proposals would provide a further safeguard to ensure that where no exception or exemption applies, the degrouping charge will not result in economic double taxation.

1.17 Annex B of this consultation document contains draft legislation for each of the proposals.

1.18 The Government would like to hear the views of business, as well as the views of representative bodies and tax advisers, on the proposals detailed in this consultation document, in order to develop fully a package of measures, with a view to legislating at the earliest practical opportunity. Chapters 2 – 4 of this document contain a number of key questions, which are summarised in Chapter 5, along with some more general questions.

2 Capital losses after a change in ownership

Background

2.1 'Capital loss buying' is a term used to describe any scheme in which a company ('Loss Co') is acquired by a new group primarily for the purpose of securing access to its capital losses, whether these are realised or latent. The loss-buying rules contained in Schedule 7A TCGA were enacted in 1993 as a measure to prevent companies from being able to access losses that arose in a company in another group, to set against their own capital gains.

2.2 The losses in question may have arisen before Loss Co joined the group, or they may arise on a subsequent disposal of an asset which Loss Co brings into a group. The rules in Schedule 7A limit the scope for capital loss buying, but they do not contain a purpose test and so are not confined to cases where a group acquires a company primarily to obtain the benefit of realised or unrealised capital losses. The rules also provide a mechanism for 'streaming' losses. This ensures that relevant losses can, broadly, only be used against gains on assets that were owned by the company (i.e. Loss Co) when it joined the group, or against assets acquired subsequently which are used for a trade conducted by the company when it joined the group.

Overlap with Targeted Anti Avoidance Rule

2.3 In Finance Act 2006, the Government introduced three Targeted Anti-Avoidance Rules (TAARs), each dealing with different aspects of tax avoidance schemes involving capital losses. The second of the TAARs, at section 184A TCGA, provides a comprehensive defence against capital loss buying. The capital loss buying TAAR was necessary because of a significant increase in the number of avoidance schemes specifically designed to circumvent the mechanical rules in Schedule 7A TCGA.

2.4 Consequently, there is now an overlap in the functions of the old Schedule 7A and the capital loss buying TAAR. The TAAR applies in precedence to the old rules, but only in cases where there is an intention to secure a tax advantage. Schedule 7A rules have continued to apply in all other cases, providing the basic rules for determining how capital losses are treated following mergers or acquisitions. Consequently, those rules are not restricted to cases involving tax avoidance.

Partial repeal of Schedule 7A

2.5 Following discussions with stakeholders, the Government believes that some of the previous loss buying rules in Schedule 7A can be repealed, resulting in much simpler legislation. This can be achieved in a number of ways, but essentially it is possible because one of the main purposes of the old rule, to provide protection against deliberate tax avoidance, is now covered by the TAARs. In practice, the sole remaining function of the old rules is to provide a rule to stream the losses of a company joining a new group.

2.6 In the context of assets acquired by a company following a change in ownership, the residual streaming function of the old rules allows pre-entry losses only against such assets that are used for a trade conducted by the company when it joined the group. Discussions with stakeholders indicated that the narrow reference to 'trade' in this condition could usefully be widened to 'trade or business'.

2.7 The July 2009 discussion document included an option to repeal the rules in Schedule 7A without replacement,[4] thus removing the streaming function of the rules entirely. However, the Government has determined that this option would result in an unacceptable Exchequer cost.

2.8 The July 2009 discussion document contained another option,[5] to align the definition of a change of ownership in these rules with that in the loss-buying TAAR. However, following further discussions with stakeholders, the Government regards this option as unnecessary, and as a result no changes are proposed to the fundamental approach of the Schedule 7A rules.

2.9 Responses to the discussion document included the suggestion to introduce a de mininis limit for the streaming of realised losses. However, a meaningful limit would necessarily involve an Exchequer cost, and so the Government's proposals do not include a de minimis limit.

Proposals

2.10 The Government's main proposal is to repeal those parts of Schedule 7A TCGA that deal with losses that have not been realised at the time when a company joins a group. It is the treatment of such losses that creates much of the complexity in the existing legislation and causes difficulty for groups that have to identify whether and where the rules apply. To maintain protection of the UK tax base, however, the Schedule will continue to apply to stream losses that are realised before a company joins a group when there is a commercially-motivated merger or acquisition (with the TAARs applying in the event of a tax-motivated merger or acquisition).

2.11 The Government is also proposing to provide greater clarity within the current, highly complex, parts of Schedule 7A that deal with situations where a company has several changes of ownership, and losses are incurred at various times so that rules are required to determine the extent to which streaming of their use applies. The proposal is not intended to amount to a change in the effect of existing law, but does seek to remove any areas of doubt through clearer drafting.

2.12 A further proposal is for the amended rules to allow restricted losses to be used against gains arising on assets used in the business carried on by a company when it joins a group rather than, as now, have this apply only in the case of assets used for trades.

2.13 The Government considers that the proposed changes would achieve a clear benefit in terms of simplification, as groups would no longer be required to make time-apportionment calculations on loss-bearing assets acquired as a result of a merger or acquisition, or have to apply complex rules for pooled assets such as shareholdings. A further benefit of the measure would be to improve the alignment between tax and economic outcomes.

2.14 Annex B contains draft legislation setting out these proposals.

Questions

- Given that Government does not believe that a complete repeal of Schedule 7A is a viable option, do you agree that the new scheme proposed above represents a worthwhile simplification of the rules?

[4] Option 3D

[5] Option 3B

- Are there other aspects of the rules which have not yet been considered that you believe could be further simplified, while retaining an effective means to stream the use of pre-entry losses?
- Do you agree that the revisions to the rules applying to situations where a company undergoes more than one change of ownership provide greater clarity?
- Do you agree that the revisions to the rules governing situations where a company undergoes more than one change of ownership do not create any material change in the current rules? If not, please give details of any changes that you consider arise.

3 Value shifting and depreciatory transactions

Background

3.1 'Value shifting' refers to the reduction in the value of an asset. In the case of a company, this will usually take place when an asset is transferred at other than its market value, which often happens where the parties are part of the same economic entity (i.e. a corporate group), or when a dividend is paid to shareholders.

3.2 Where a company has lost value in this way, there are two capital gains rules that may take account of the consequences when shares in that company are subsequently sold. One rule is at section 30 TCGA and the other is at section 176 TCGA.

3.3 Section 30 TCGA addresses tax avoidance involving value shifting. However, this rule is subject to the restrictions in sections 31 to 34 where the value reduction results from certain transactions within groups of companies. This is because section 30 is essentially a mechanical provision that may in some circumstances impose an additional charge following normal commercial transactions within a group, even when the economic gain to the group is fully recognised in calculating the chargeable gain on a subsequent share disposal. It is these specific provisions that are generally referred to as the "value shifting rules". They are designed to counter tax driven arrangements such as the "drain out dividend scheme".[6] These rules can adjust both a gain and a loss.

3.4 Section 176 TCGA (extended to non-group situations by section 177) deals with situations where a loss arises, or is increased, when shares are sold after the value of a company has been reduced in similar ways to those described in the paragraph above. When shares in a company are disposed of following such a transaction, then without this rule a tax loss could arise when there is in fact no economic loss. Such a situation could arise following entirely routine commercial transactions. The provision at section 176 is known as the "depreciatory transactions rule". It can reduce or eliminate a loss but cannot create or increase a gain.

3.5 There is some overlap between the value shifting rules and the depreciatory transactions. However, unlike the value shifting rules, the depreciatory transactions provisions cannot convert a loss into a gain, or increase the amount of a gain. They simply deal with a consequence of having a corporate structure, rather than with tax driven transactions, as shown in the following examples.

Depreciatory transactions – examples

3.6 In both of the following examples, it is supposed that the shares in the company initially cost £1000 in total.

[6] Where a valuable company receives a loan to provide funds, which are then paid out as a dividend. The company is then of low value and is sold for little. The vendor receives the repayment of the loan following the sale, rather than direct sale consideration.

- **Example 1 – a gain in company value.** The company rises in value to £1,800 and an asset worth £500 is taken out before the company is then sold for £1,300. In the absence of any other features, the tax result follows the economic result: there is a profit of £300.
- **Example 2 – a loss in company value.** The company rises in value to £1,200. An asset worth £900 is taken out of the company, and then the company is sold for £300. There may not be any economic loss in this situation. Without the depreciatory transactions provisions, there would be a tax loss of £700; the depreciatory transactions provisions ensure that the loss is eliminated.

Issues identified

3.7 Business representatives have identified the value-shifting rules that apply to transactions within groups of companies (sections 31to 34 TCGA) as being particularly burdensome when considering commercial disposals. These provisions can lead to time-consuming work both in identifying whether there are any past transactions that might trigger the rules and in deciding whether there would be a consequential tax effect. The complexity of the rules means that taxpayers will sometimes seek specialist advice, but even so, some representatives remained uncertain of the effect of the legislation (or whether HMRC would seek an adjustment) in respect of particular transactions.

3.8 The Government recognises that the value shifting rules can be burdensome for companies and that they are a priority for simplification.

Time limits

3.9 In addition, the Government accepts that the absence of any time limit to the effect of the depreciatory transaction provisions (sections 176 and 177 TCGA) can cause onerous compliance burdens, because of the need to review historic commercial transactions.

3.10 Apart from the absence of a time limit, responses from business indicated that the depreciatory transaction rules work well: they are well understood and regarded as straightforward to apply, in contrast to the value shifting rules.

3.11 The Government notes that the targeted anti-avoidance rule (TAAR) dealing with the creation of artificial losses at section 16A TCGA provides further revenue protection where transactions have been undertaken with the objective of creating a capital loss. The Government's view is that the TAAR should continue to apply without any time limit so as to maintain a robust safeguard against tax avoidance.

Further considerations

3.12 The Government notes that while a depreciatory transaction adjustment might be appropriate to adjust the effect of entirely commercial transactions, the value shifting provisions address differences between economic and fiscal outcomes that can result from tax planning activity. An example of such activity is the "drain out dividend" scheme mentioned above, which led to section 30 TCGA being extended to cover disposals that followed reductions of value within a group of companies.

3.13 In light of the above, the Government does not believe that the option outlined in the July discussion document[7] to extend the depreciatory transaction rules to apply to gains as well as losses would achieve simplification. This is because additional rules would be required to limit the effect of any new depreciatory transactions provisions on the computation of gains. Nor would it be straightforward to produce a simpler mechanical rule that would also provide certainty.

3.14 The Government considers that replacing the existing value shifting rules that affect transactions within groups with a tightly focused TAAR will provide business with greater certainty about the application of such rules. The proposed TAAR would apply where transactions have taken place that artificially reduce the value of a company compared to its true value to a purchaser. Further simplification can be achieved by having this rule apply to corporation tax resulting from all disposals by companies of shares rather than, as now, having section 30 apply (without the various modifications of sections 31 to 34) in various circumstances.

3.15 Previous experience suggests that a new TAAR would be an appropriate means to achieve simplification: the TAARs applying to corporate capital losses, introduced in 2005, appear to be well understood. They provide the revenue protection that the Government requires and give certainty to business.

Proposals

Value Shifting

3.16 An adjustment under the value shifting provisions in the group context is appropriate where tax-driven transactions have taken place that have artificially reduced the value of a company compared to the true value to a purchaser. Given this, the Government considers that certainty for business can be achieved by introducing a motive based rule, tightly targeted on transactions that are designed to produce a tax advantage in terms of corporation tax on chargeable gains.

3.17 The focus of the proposed rule would be on the motive and effect of transactions undertaken rather than, as now, on the precise means by which a reduction in value is achieved. An entirely separate rule would apply to the vast majority of disposals of shares and securities by companies,[8] removing any overlap with section 30. Under the proposal, the new value shifting provisions would apply where there have been arrangements that reduce the value of shares and that a main purpose of those arrangements is to obtain a tax advantage in terms of corporation tax. Because the effect of the rule would be to adjust the consideration received for capital gains purposes, the rule will only apply where a tax advantage is obtained in relation to capital gains.

3.18 The new rule would provide for the 'look through' of group transactions, as at present. The Government has taken the opportunity to simplify the application of the rule to, and the interaction with, the degrouping charge.

3.19 The new rule would be closely targeted at tax avoidance, and for this reason, consistently with other targeted anti-avoidance measures, the Government proposes that there would be no time limit in terms of the period between the transactions being undertaken and the disposal affected.

[7] Option 4A

[8] Under the Government's proposal, the new rules would apply only to corporation tax, so section 30 TCGA would continue to apply to the sale of shares by a company in a fiduciary company

3.20 The Government considers that the definition of "arrangements" and the inclusion of a purpose test in the draft legislation, is sufficient to ensure that the rule will not apply where the consideration for the sale of shares is reduced simply because the company has paid a dividend out of its profits in the normal way.

3.21 Any business undertaking purely commercial transactions that are not motivated by tax avoidance would not need to consider the effect of such a rule.

3.22 Annex B contains draft legislation setting out these proposals.

Depreciatory transactions

3.23 Given that the depreciatory transactions legislation can apply to transactions that are wholly commercial in nature, in addition to tax motivated transactions, the Government recognises the case for a time limit. It considers that compliance burdens can be reduced consistently with maintaining revenue protection, by the introduction of a limit of six years between the time of the depreciatory transaction and the subsequent disposal of shares.

3.24 Other than introducing a six year time limit, the Government's proposal would leave the depreciatory transactions rules, which are currently well understood by business, unaltered.

Questions

- Do you consider that the attached draft legislation is effectively targeted against transactions that are designed to produce a tax advantage?
- Would the attached legislation provide appropriate reassurance for taxpayers undertaking commercial transactions?
- Are there specific circumstances or examples that you would like HMRC to cover in guidance to show how the legislation applies?

4 Degrouping charges

Background

4.1 Assets transferred between companies within the same capital gains group are generally treated as taking place at a value that creates neither a gain nor a loss for tax purposes. Recognition of a taxable gain or loss on the disposal of the asset is deferred until such time as the asset is disposed of outside the group.

4.2 Since 1968, the "degrouping charge" rule (section 179, TCGA) has ensured that if a company leaves its group with an asset acquired from a fellow group member within the last six years, any gain or loss deferred from an earlier date is reinstated. As such, its purpose is to ensure that a tax charge arises whenever a company leaves a group having recently acquired an asset from another group company and to counteract any tax advantage that might otherwise be obtained by asset transfers within the group.

4.3 Discussions with business have indicated widespread acknowledgement that some form of degrouping charge is necessary to protect the tax system. Without such a charge it would be possible to avoid corporation tax on profits from the sale of assets, for example by transferring an asset into a newly incorporated company whose shares have been set up with a high tax base cost, and then selling the company (rather than directly selling the asset) so that there is no gain. Widespread use of such arrangements led to the introduction of the charge.

Issues identified

4.4 There are a number of separate features of the current degrouping charge rules that together place a significant burden on groups, especially when an acquisition or disposal of all or part of a group's activities is being contemplated.

Interaction with Substantial Shareholding Exemption

4.5 A significant concern with the current degrouping charge rules, expressed by a number of business representatives, is the way that these rules interact with the provisions in the SSE in Schedule 7AC TCGA. A degrouping charge may arise in respect of a trade asset owned by a trading company, yet the share sale which gives rise to the degrouping event would itself be an exempt disposal for chargeable gains purposes by virtue of the provisions in the SSE. The imposition of a degrouping charge in respect of an asset used for a trade in an otherwise exempt sale was one of the major irritants highlighted by business representatives. This particularly concerned groups that organise their business on a divisionalised basis. Although a disposal of a single business will often involve putting assets into a group company prior to sales, the benefits of the SSE may not be available. Stakeholders could see no justification for preventing the exemption applying in cases involving this type of restructuring before a sale.

4.6 As noted in the July 2009 discussion document, in order to be fully effective for divisionalised businesses that restructure in advance of a business disposal, this option would also require an amendment to the rules in Schedule 7AC TCGA regarding the period of time that the company has carried on the trade prior to disposal, so that account is taken of periods where the trade is carried on by other members of the group.

4.7 In particular, this would mean that in cases where assets that have been used for the purposes of a trade by the group are transferred to a newly incorporated company that continues to use them for a trade, the condition requiring that the investing company have held shares in a trading company for a period of 12 months would be modified.

Economic double taxation

4.8 One issue highlighted by discussions with stakeholders is that economic double taxation can potentially arise as a result of the operation of the degrouping charge rules with gains on both the transferred asset and the share disposal being subject to tax. The rules are mechanical, with no test of purpose, and no mechanism to reduce the amount of a charge where double taxation would arise.

4.9 There may be no tax advantage if a group asset is sold to an existing group company that is later sold, but there may be one where a newly created company is used, even if this is for commercial reasons. In particular, for a single asset company a tax advantage may arise where the cost of the shares in the company sold is equivalent to the value of the asset transferred. However companies owning just a single asset are often sold solely for commercial reasons. For example, property sales often occur in this way, in order to maintain the continuity of leases to tenants. Transferring assets around a group – particularly before a re-organisation or demerger – is a common commercial practice and the complexity of the degrouping charge rules mean that there is a significant compliance and administrative cost to groups in ensuring that this does not give rise to economic double taxation.

Liability for degrouping charge

4.10 A concern expressed by some stakeholders is that the current degrouping charge could be seen to be targeting the wrong company. At present, a chargeable gain falls on the company leaving the group and owning the asset. However, the economic gain being taxed arose during the period in which the asset was owned by the company that previously transferred the asset. A consequence of the current rule is that any tax due is payable by the company that has left the original group. There will almost inevitably be commercial arrangements in place for the vendor group to reimburse the purchaser for any tax charge; alternatively, the vendor and purchaser group companies can jointly agree to make an election under the degrouping rules to transfer the gain to another company in the vendor group. However, dialogue with stakeholders has indicated that it may not be possible to review all historic transactions to determine potential degrouping charges by the time of the disposal.

4.11 The Government's proposal would ensure that in these circumstances, the tax is initially payable by the vendor group, rather than by the company that has been transferred. This outcome would be achieved by treating the degrouping charge not as a separate charge in that company, but as an adjustment to the taxable profit or loss on the sale of the shares that causes the company to leave the group.

Time limits

4.12 A feature of the degrouping charge rules commonly cited in discussions and in written responses to the July 2009 discussion document was whether a six year time limit was necessary, or whether a shorter limit would suffice for revenue protection purposes. This was included as one of the options in the discussion document. However, the Government considers that retaining this time limit will achieve an appropriate balance between minimising compliance burdens and protecting revenue. The six year limit will be consistent with the new time limit proposed for the application of the depreciatory transactions rules (as outlined in Chapter 3).

Associated companies exception

4.13 When degrouping charges were first introduced, the potential for double taxation of gains was identified, and an exception was provided that was intended to address this, at least in the majority of circumstances. This is the "associated companies" exception in section 179(2) TCGA, which can switch off the degrouping charge rules where the only asset transfers that have taken place are within a sub-group of companies that are all sold together. In such circumstances there should be no risk of tax avoidance being present because the asset transfers should not have moved value in to, or out of, any companies other than those included in the sale.

4.14 The associated companies exception has commonly been relied on to "switch off" potential double charges in the past. However, following a recent case heard by the Court of Appeal[9] there was a great deal of comment in the professional media that indicated there were clear differences of opinion about the way in which this exception is to be applied. Even where the exception is applied according to the interpretation preferred by HMRC, it can require some commercially unnecessary actions to achieve the desired tax outcome. One example cited by stakeholders is that where the activities of a group company are being wound up and its assets are transferred to other group companies, the dormant shell company cannot safely be liquidated for six years. This is because the transferee company must still exist if the associated companies exception is to be applied on a later sale of the consolidated business.

Proposals

4.15 Under the Government's proposals, the amount of a degrouping charge would be calculated broadly as it is under current legislation, corresponding to the amount of any gain (or loss) that has been deferred as a result of previous intra-group transfers. However, in situations where - as will typically be the case - an asset-holding company leaves the group because of a disposal of shares by a group company, effect would be given to the degrouping charge, by way of an addition to the consideration for the disposal of shares (where there is a degrouping gain), or by way of an increase in the costs allowable as a deduction (where there is a degrouping loss). As a consequence, any exemption or relief that might apply to the share disposal, such as the SSE, will also apply to the degrouping charge.

4.16 Where two or more shares disposals happen at the same time, and a degrouping charge arises, the proposals would give considerable freedom to groups in determining to which disposal(s) the adjustment is applied. This can happen where more than one company makes a disposal of the shares or where there is more than one class of share disposed of by a single company.

4.17 Where a company leaves a group otherwise than as a result of a disposal of shares, such as following an issue of new shares, and there is potentially a degrouping charge in relation to certain assets, then any degrouping charge would arise as a stand alone charge in the asset holding company, as at present.

4.18 Where assets that have been used for the purposes of a trade by the group are transferred to a company then the current requirement that the investing company must have held shares for a period of 12 months for the SSE to apply will be modified. The investing company would be treated as having the necessary holding of shares in a qualifying company for the period that those assets were being used for a trade conducted by the group. This would allow the exemption to apply when trading activities are placed within a newly incorporated group company which is then sold out of a trading group, to the benefit of groups that have various trading activities conducted within single companies.

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[9] See Johnston Publishing (North) Ltd v Revenue and Customs Commissioners [2008] EWCA Civ 858; [2008] WLR (D) 253

4.19 To prevent economic double taxation, the proposal makes provision for the degrouping charge to be reduced where doing so is just and reasonable, taking into account the level of share capital of the companies being sold, and the circumstances under which the company leaving the group acquired the asset. Such a reduction is to be made following a claim. Assuming that the proposal is taken forwards, HMRC will issue detailed guidance with examples of the circumstances where such a claim might be expected. It is envisaged that the ability to make such a claim will, for example, negate the need for groups to retain dormant companies solely for the purposes of ensuring that they can take advantage of the revised associated companies exception. Claims under this provision would only be necessary where any liability remains after considering whether any exemption or relief, such as the SSE, is available.

4.20 In line with the considerations listed at paragraph 4.12 above, the time limit for the application of the degrouping charge would remain at six years.

4.21 To remove existing uncertainty concerning the application of the associated companies exception to the degrouping charge, as outlined in paragraph 4.14 above, HMRC's view of the application of the current legislation, with additional clarity for areas where recent tax cases have not provided guidance, would be set out in law. The Government's proposal is to replace the existing subsection (2) of section 179 TCGA with a rule that will disapply the degrouping charge rule where two companies are in the same 'subgroup' at all times between the date of the transfer of an asset from one to the other until immediately after both leave the original group.

4.22 In response to stakeholder comments, the Government proposes that the same rule for the new exception would also be introduced for degrouping charges arising under the intangible fixed assets regime in Part 8 of the Corporation Tax Act 2009.

4.23 The changes outlined above will provide an effective exemption for degrouping charges on many trade asset disposals where these are part of a share disposal that qualifies for the SSE. Asset level disposals of trade assets, while not generally exempted, can often benefit from the business asset roll-over relief in sections 152 – 160 TCGA. It is the Government's view that the additional facility to roll-over a degrouping charge provided in section 179B (and supplementary provisions in Schedule 7AB) are rendered largely redundant. Consequently, the proposal includes the repeal of these provisions.

4.24 The changes proposed above would also enable the repeal of the separate provision that allows a degrouping charge to be transferred between group companies. To replace this separate provision, section 171A would be amended so that it also applies where necessary to instances where there is still a 'stand-alone' degrouping gain or loss.

4.25 Finally, the Government proposes a minor amendment to the existing rules that would ensure a degrouping charge (or adjustment to a charge on a share disposal) is only made where companies are both members of the same group at the time that an asset is transferred between the two companies.

4.26 Annex B contains draft legislation setting out these proposals.

Questions

- What benefits or otherwise do you see arising from the proposal to treat most degrouping charges as adjustments to the computation of gains or losses from a share disposal? Where appropriate, please consider any impacts on transactional costs, administrative burdens and tax compliance costs.

- The proposals include a rule for reallocating degrouping gains and losses between disposals by different companies and between different classes of shares. Do you think this could be simplified? If so, please explain how.
- Do you agree that the revision to the rules relating to the old "associated companies" exception provides a clear and unambiguous rule?
- Are you content that the 'backstop' rule to prevent economic double taxation would be sufficient to address the issue, both from a technical and practical viewpoint?
- Are there particular examples that you would wish HMRC to address in guidance to demonstrate how the 'backstop' rule would operate?
- Do you agree that the proposals to repeal section 179A, 179B and Schedule 7B TCGA are appropriate given the scope of the changes elsewhere in these proposals? If not, please explain why you believe an alternative course would be better.

5 Questions for consideration

5.1 The Government welcomes views from groups of companies and their representatives, in addition to the views of professional advisers, on the questions asked in this consultation document.

General questions

1 Do you agree that the proposed changes would deliver closer alignment between tax and economic outcomes?

2 Do you see any particular technical issues that need to be resolved in any of the draft legislation, that have not yet been addressed?

3 Do you consider the attached draft legislation to be as clear as possible? If not, where could it be made clearer, and how?

Impact Assessment

4 We would be grateful for any information relating to the administrative savings and/or the reduction in transaction/compliance costs that you would expect to result from this draft legislation. The consultation stage Impact Assessment for each set of proposals can be found at:

http://www.hm-treasury.gov.uk/consult_simplification_capitalgains.htm

Capital losses after a change in ownership

5 Given that Government does not believe that a complete repeal of Schedule 7A is a viable option, do you agree that the new scheme proposed represents a worthwhile simplification of the rules?

6 Are there other aspects of the rules that you consider could be further simplified while retaining an effective means to stream the use of pre-entry losses?

7 Do you agree that the revisions to the rules governing situations where a company undergoes more than one change of ownership provide greater clarity than the present rules?

8 Do you agree that the revisions to the rules governing situations where a company undergoes more than one change of ownership do not create any material change in the current rules? If not, please give details of any changes that you consider arise.

Value shifting and depreciatory transactions

9 Do you consider that the attached draft legislation is effectively targeted against transactions that are designed to produce a tax advantage?

10 Would the attached legislation provide appropriate reassurance for taxpayers undertaking commercial transactions?

11 Are there specific circumstances or examples that you would like HMRC to cover in guidance to show how the legislation applies?

Degrouping charges

12 What benefits or otherwise do you see arising from the proposal to treat most degrouping charges as adjustments to the computation of gains or losses from a share disposal? Where appropriate, please consider any impacts on transactional costs, administrative burdens and tax compliance costs.

13 The proposals include a rule for reallocating degrouping gains and losses between disposals by different companies and between different classes of shares. Do you think this could be simplified? If so, please explain how.

14 Do you agree that the revision to the rules relating to the old 'associated companies' exception provides a clear and unambiguous rule?

15 Are you content that the 'backstop' rule to prevent economic double taxation would be sufficient to address the issue, both from a technical and practical viewpoint?

16 Are there particular examples that you would wish HMRC to address in guidance to demonstrate how the 'backstop' rule would operate?

17 Do you agree that the proposals to repeal section 179A, 179B and Schedule 7B TCGA are appropriate given the scope of the changes elsewhere in these proposals? If not, please explain why you believe an alternative course would be better.

6 Next steps

How to respond

6.1 The Government welcomes answers to the questions listed in Chapter 5 and any wider comments on the proposals in this consultation document. Responses should be sent to:

The Related Companies Simplification Review Team
Room 2/E1
HM Treasury
1 Horse Guards Road
London, SW1A 2HQ

Alternatively, please email: relatedcompanies.simplification@hmtreasury.gsi.gov.uk

Telephone enquiries: 020 7270 6104

6.2 Comments should be received by 17 May 2010.

Proposed workshop

6.3 The Government intends to hold a workshop to discuss stakeholder views and any further ideas, before the end of the 12 week consultation period. Please send your expressions of interest to the e-mail address above and indicate your preferred dates by 12 March 2010. You will receive a reply by email with details on when and where the workshop will be held.

Confidentiality disclosure

6.4 Information provided in response to this discussion document, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

6.5 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarding as binding on HM Treasury or HM Revenue & Customs (HMRC).

6.6 HM Treasury and HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

A The Government's Code of Practice on consultation

About the consultation process

This consultation is being conducted in accordance with the Government's Code of Practice on Consultation. If you wish to access the full version of the Code, you can obtain it online at:

http://www.berr.gov.uk/files/file47158.pdf

The consultation criteria

1. When to consult - Formal consultation should take place at a stage when there is scope to influence the policy outcome.

2. Duration of consultation exercises - Consultations should normally last for at least 12 weeks with consideration given to longer timescales where feasible and sensible.

3. Clarity of scope and impact - Consultation documents should be clear about the consultation process, what is being proposed, the scope to influence and the expected costs and benefits of the proposals.

4. Accessibility of consultation exercise - Consultation exercises should be designed to be accessible to, and clearly targeted at, those people the exercise is intended to reach.

5. The burden of consultation - Keeping the burden of consultation to a minimum is essential if consultations are to be effective and if consultees' buy-in to the process is to be obtained.

6. Responsiveness of consultation exercises - Consultation responses should be analysed carefully and clear feedback should be provided to participants following the consultation.

7. Capacity to consult - Officials running consultations should seek guidance in how to run an effective consultation exercise and share what they have learned from the experience.

If you feel that this consultation does not satisfy these criteria, or if you have any complaints or comments about the process, please contact:

Richard Bowyer, Better Regulation Unit
Email: richard.bowyer@hmrc.gsi.gov.uk
Telephone: 020 7147 0062

B Draft legislation

Capital losses after a change in ownership

Draft legislation below

SCHEDULE 1

Section {j1320}

CORPORATE TAX ON GAINS: LOSSES AFTER CHANGE OF OWNERSHIP [J1320S]

TCGA 1992

1 In section 177A of TCGA 1992 (restriction on set-off of pre-entry losses), omit "and losses accruing on assets held by any company at such a time".

2 Schedule 7A to that Act (restriction on set-off of pre-entry losses) is amended as follows.

3 In paragraph 1 (application and construction of Schedule)—

(a) for sub-paragraph (2) substitute—

"(2) In this Schedule "pre-entry loss", in relation to any company, means any allowable loss that accrued to that company at a time before it became a member of the relevant group.",

(b) omit sub-paragraphs (3), (3A), (4) and (5),

(c) in sub-paragraph (6) for "Subject to" to "if" substitute "If", and

(d) omit sub-paragraph (8).

4 Omit paragraphs 2 to 5 (determination of pre-entry proportion of losses on pre-entry assets).

5 In paragraph 6 (restrictions on the deduction of pre-entry losses)—

(a) in sub-paragraph (2)—

(i) omit paragraph (a) (and the "and" after it), and

(ii) in paragraph (b), omit "in any other case", and

(b) in sub-paragraph (3)—

(i) omit paragraph (a) (and the "and" after it), and

(ii) in paragraph (b), omit "in the case of an election under sub-paragraph (2)(b) above,".

6 In paragraph 7 (gains from which pre-entry losses are to be deductible)—

(a) in sub-paragraph (1), in paragraph (c)(ii) after "trade" insert "or business",

(b) after that sub-paragraph insert—

"(1A) Where a company, having become a member of the relevant group, subsequently becomes a member of another group ("the new group")—

(a) sub-paragraph (1) continues to have effect, in relation to any loss which accrued to the company before it became a member of the relevant group, by reference to the date on which it became such a member, and

(b) accordingly, that sub-paragraph does not apply separately in relation to the loss by reason of it also having accrued to the company before it became a member of the new group.",

(c) omit sub-paragraph (2),

(d) in sub-paragraph (3) omit—

(i) ", without prejudice to paragraph 9 below",

(ii) paragraph (b), and

(iii) in paragraph (c), "and (2)(c)",

(e) for sub-paragraph (4) substitute—

"(4) Sub-paragraphs (4A) and (4B) apply for determining for the purposes of this paragraph whether an asset on the disposal of which a chargeable gain accrues was an asset held by a company immediately before the date on which it became a member of the relevant group (a "pre-entry asset").

(4A) Except as provided by subsection (4B), an asset is not a pre-entry asset if—

(a) the company which held the asset at the entry date is not the company which makes the disposal, and

(b) since the entry date that asset has been disposed of otherwise than by a disposal to which section 171 applies.

(4B) Without prejudice to sub-paragraph (4C), where, on a disposal to which section 171 does not apply—

(a) an asset would cease to be a pre-entry asset by virtue of sub-paragraph (4A), but

(b) the company making the disposal retains an interest in or over the asset in question,

that interest is a pre-entry asset.

(4C) For the purposes of this paragraph—

(a) an asset acquired or held by a company at any time and an asset held at a later time by that company, or by any company which is or has been a member of the same group of companies as that company, is to be treated as the same asset if the value of the second asset is derived in whole or in part from the first asset, and

(b) if—

(i) any asset is treated (whether by virtue of paragraph (a) or otherwise) as the same as an asset held by a company at a later time, and

(ii) the first asset would have been a pre-entry asset in relation to that company,

the second asset is also to be treated as a pre-entry asset in relation to that company;

and paragraph (a) applies, in particular, where the second asset is a freehold and the first asset is a leasehold the lessee of which acquires the reversion.",

(f) in sub-paragraph (5) omit "or (2)" (in both places), and

(g) in sub-paragraph (6) omit "or (2)".

7 In paragraph 8 (change of a company's nature)—

(a) in sub-paragraph (1)—

(i) after "trade" (in each place) insert "or business", and

(ii) omit "and (2)(c)",

(b) for sub-paragraph (2) substitute—

"(2) In sub-paragraph (1) "a major change in the nature or conduct of a trade or business" includes—

(a) a major change in the type of property dealt in, or services or facilities provided, in the trade or business,

(b) a major change in customers, markets or outlets of the trade or business, or

(c) in the case of a company with investment business (within the meaning of section 1218 of CTA 2009), a major change in the nature of the investments held;

and this paragraph applies even if the change is the result of a gradual process which began outside the period of three years mentioned in sub-paragraph (1)(a)."

8 Omit paragraph 9 (identification of "the relevant group" and application of Schedule to every connected group).

9 In paragraph 11 (continuity provisions), omit sub-paragraph (3)(b) (and the "and" before it).

Consequential provision

10 Omit the following provisions (which relate to the provisions repealed by paragraphs 1 to 9)—

(a) in FA 1994, sections 93(8) to (10) and 94;

(b) in FA 1998, section 138;

(c) in FA 2000, in Schedule 29, paragraph 7(2) to (5);

(d) in F(No 2)A 2005, section 65(2), (3) and (5).

Commencement

11 (1) The amendments made by this Part of this Schedule have effect on and after commencement in relation to the deduction of any pre-entry loss within paragraph 1(2)(a) of Schedule 7A to TCGA 1992 (as amended by this Part) regardless of—

(a) whether the loss accrued before or on or after commencement, and

(b) whether the company which accrued the loss became a member of the relevant group (within the meaning of that Schedule) before or on or after commencement.

(2) In this paragraph "commencement" means the time when this Act is passed.

Transitional provision

12 (1) Sub-paragraph (2) applies where, immediately before commencement, Schedule 7A to TCGA 1992 had effect, in the case of a company which is or has been a member of a group of companies ("the relevant group") in relation to a loss of that company within paragraph 1(2)(b) of that Schedule (pre-entry proportion of an allowable loss that has accrued to a company on the disposal of a pre-entry asset).

(2) On and after commencement that loss is to be treated, for the purposes of Schedule 7A to TCGA 1992, as if it were a pre-entry loss within the meaning of paragraph 1(2) of that Schedule (as substituted by paragraph 3 of this Schedule) which accrued to that company immediately before it became a member of the relevant group.

(3) In this paragraph "commencement" means the time when this Act is passed.

EXPLANATORY NOTE

SCHEDULE [XX] : CORPORATE GAINS (SIMPLIFICATION): RESTRICTION ON SET OFF OF PRE-ENTRY LOSSES

SUMMARY

1. Schedule [XX] simplifies the current rules that apply to restrict the circumstances in which capital losses of a company that joins a group can be set against gains. In particular, the use of losses that arise after a company joins a group will no longer be restricted. Losses that are restricted may be used against gains arising on assets used in the same business that the company conducted before joining the group rather than, as now, only against gains on assets used in the same trade. The changes apply to the deduction on or after the passing of the Act of any loss that accrued before a company joined a group.

DETAILS OF THE SCHEDULE

2. Paragraph 3 of Schedule [XX] amends the definition of a "pre-entry loss" for the purposes of Schedule 7A Taxation of Chargeable Gains Act 1992 so that it only applies to the losses of a company that accrue before it becomes a member of a group.

3. Paragraphs 3 and 4 remove from Schedule 7A all of those parts that restrict the capital losses of a company that accrue after it becomes a member of a group.

4. Paragraph 5 amends paragraph 6(2) of Schedule 7A. This provides a procedure by which, in certain circumstances, a company can elect whether it is restricted "pre-entry losses" or other losses which have been allowed against gains. The change reflects the more limited circumstances in which a loss may be restricted.

5. Paragraph 6(a) extends the circumstances in which a restricted loss may be used to include setting off against gains arising on assets used in any trade or business that was carried on by the company before it joined the group.

6. Paragraph 6(b) inserts into Schedule 7A a new paragraph 7(1A) which sets out clearly the rule that once a loss has become subject to restriction under the Schedule then the same restriction continues to apply should the company subsequently join another group.

7. Paragraph 6(c) amends paragraph 7 of Schedule 7A to set out a definition of "pre-entry asset", the gains on which may be have restricted losses deducted. The definition previously depended on the rules for restricting losses that accrue after the company join the group, which have been repealed.

8. Paragraph 7 amends paragraph 8 of Schedule 7A which applies to the use of restricted losses where there has been a major change in the activity of a company after it joins a group. The changes take account of the extension of the use of restricted losses to gains on assets used for a continuing business, rather than just a continuing trade.

9. Paragraph 11 sets out the commencement provision. The new rules apply to the deduction on or after the passing of the Act of any loss that accrued before a company joined a group.

10. Paragraph 12 is a transitional provision. Where a loss on the disposal of an asset after a company joined a group is subject to restriction under the current rule, then it will be treated as one that arose before the company joined the group for the purposes of the amended rules.

BACKGROUND NOTE

11. The revised Schedule will reduce compliance costs by simplifying the rules that apply to restrict the use of losses when a company joins a group.

12. The amended rules will apply a restriction only to losses that have been realised before the company joins the group and will also allow restricted losses to be used against gains in a continuing business rather than only against those in a continuing trade.

13. The changes are made in response to consultation on capital gains group simplification. The existing scope of the restrictions is no longer acquired because the tax motivated acquisition of companies with losses is addressed by a targeted anti-avoidance rule at Section 184A TCGA.

Value shifting and depreciatory transactions

Draft legislation

SCHEDULE 1 Section {j1310}

CORPORATION TAX ON CAPITAL GAINS: VALUE SHIFTING [J1310S]

1 In section 30 of TCGA 1992 (tax-free benefits)—
(a) in subsection (1)(a) omit "or a relevant asset",
(b) for subsection (2) substitute—

"(2) But, for the purposes of corporation tax, this section does not have effect if the disposal of the asset is a disposal by a company of shares in, or securities of, another company (as to which see section 31).", and

(c) omit subsection (8).

2 For sections 31 to 34 of TCGA 1992 (which make provision about disposals by companies of shares in or securities of other companies) substitute—

"31 Disposal of shares or securities by a company

(1) For the purposes of corporation tax, subsection (2) has effect as respects the disposal by a company ("the disposing company") of shares in, or securities of, another company if—
(a) arrangements have been made whereby the value of those shares or securities, or any relevant asset, has been materially reduced, and
(b) the main purpose, or one of the main purposes of the arrangements is to obtain a tax advantage.

(2) Any allowable loss or chargeable gain accruing on the disposal is to be calculated as if the consideration for the disposal were increased by such amount as is just and reasonable having regard to—
(a) the arrangements, and
(b) any chargeable gain or allowable loss arising by virtue of section 179 of this Act, or section 780 or 785 of CTA 2009, in consequence of the disposal.

(3) For the purposes of subsection (1)—
(a) an asset is a relevant asset if, at the time of the disposal, it is owned by a company which is a member of the same group as the disposing company, and
(b) it does not matter whether the tax advantage is obtained for the disposing company or any other person.

(4) In relation to a case in which the disposal of the shares or securities precedes their acquisition, the reference in subsection (1)(a) to a reduction is to be read as including a reference to an increase.

(5) Where, but for arrangements to which subsection (6) applies, a transaction would, by virtue of section 29(2), be treated as a disposal of shares by a company, that transaction is to be treated as if it were, by virtue of section 29(2), a disposal of those shares.

(6) The arrangements to which this subsection applies are arrangements—
(a) whereby the value of the shares has been materially reduced, and

(b) the main purpose, or one of the main purposes of which is to obtain a tax advantage (whether for the company or any other person).

(7) In this section—

"arrangements" includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable);

"group" is to be construed in accordance with section 170;

"securities" has the same meaning as in section 132;

"tax advantage" means the avoidance of a liability to corporation tax."

3 In section 176 of TCGA (depreciatory transactions within a group), in subsection (1) for "on or after 31st March 1982" substitute "within the period of 6 years ending with the disposal".

4 In section 179 of TCGA (company ceasing to be member of group), in subsection (9)(b), after "section 30" insert "or 31".

5 (1) The amendments made by paragraphs 1 to 3 have effect in relation to disposals of shares or securities by companies made on or after the passing of this Act.

(2) But nothing in paragraph 1 or 2 prevents section 31A of TCGA 1992 (asset-holding company leaving group), as it had effect immediately before the passing of this Act, continuing to have effect on or after the passing of this Act in relation to cases where the section 30 disposal to which that section refers occurred before the passing of this Act.

(3) The amendment made by paragraph 4 has effect in relation to disposals of shares or securities treated under section 179 as taking place on or after the passing of this Act.

(4) In this paragraph "securities" has the same meaning as in section 132 of TCGA 1992.

EXPLANATORY NOTE

SCHEDULE [XX] : CORPORATE GAINS (SIMPLIFICATION): VALUE SHIFTING

SUMMARY

1. Schedule [XX] simplifies the current rules that apply where the capital gains proceeds on the disposal are reduced because the value of an asset has been reduced. The complex rules that apply to transactions involving companies are replaced by a new targeted anti-avoidance rule that applies to disposals of shares or securities by companies on or after the passing of the Act. The new rule applies where capital gains disposal proceeds are affected by tax motivated transactions. Where the rule does apply, it acts to adjust the disposal consideration to counter any tax advantage of the transactions.

DETAILS OF THE SCHEDULE

2. Paragraph 1 amends the current value shifting rule in section 30 Taxation of Chargeable Gains Act 1992 ("TCGA") to remove the parts that relate to transactions within groups and make its operation subject to section 31 onwards in relation to a disposal by a company of shares in another company. Section 30 shall no longer apply to such a disposal for the purposes of corporation tax.

3. Paragraph 2 removes the existing rules that modify section 30 at section 31 to 34 and replaces them with a new section 31 which is a self contained rule applying to disposals of shares or securities for the purposes of corporation tax.

4. New subsection (1) applies the rule where arrangements have been made that have reduced the value of shares or securities and the purpose of those arrangements was to obtain a tax advantage. It also applies where it is the value of a "relevant asset" that has been reduced.

5. New subsection (2) provides for the consideration received on a disposal to be adjusted by an amount that is just and reasonable in the light of the arrangements and the amount of any degrouping charge that arose as a result of the disposal.

6. New subsection (3) defines a "relevant asset" and ensures that the rule applies where the tax advantage is obtained by any person.

7. New subsection (4) modifies the rule in the case where the disposal of shares or securities occurs before their acquisition so as to apply where their value is increased.

8. New subsection (5) clarifies the interaction of the rule with section 29 TCGA to ensure that a capital gains disposal will result where shares are issued by a company whose value has previously been reduced by arrangements within the scope of this subsection.

9. New subsection (6) sets out the arrangements within the scope of subsection (5).

10. New subsection (7) provides definitions of “arrangement”, “group”, “securities” and “tax advantage” for the purposes of the section.

11. Paragraph 3 introduces a time limit into the depreciatory transaction rule in section 176 TCGA. An adjustment under that section may be made where a disposal takes place up to 6 years following a depreciatory transaction.

12. Paragraph 4 amends the degrouping charge rules in section 179 TCGA to allow such a charge to be adjusted by this new rule.

13. Paragraph 5 sets out the commencement provision. The amendments will apply to disposals made on or after the passing of the Act, including deemed disposals resulting from the degrouping charge in section 179 TCGA. The current section 31A has the effect of applying section 30 to create a separate charge some time after a disposal of shares and will continue to apply in the case of disposals that took place before the passing of the Act.

BACKGROUND NOTE

14. The revised schedule will reduce compliance costs for companies by simplifying the rules that apply to adjust disposal consideration where the value of shares or securities has been reduced.

15. The complex mechanical rules that currently apply to restrict the operation of section 30 TCGA will be replaced by a simple rule targeting tax motivated transactions.

16. The changes are made in response to consultation on capital gains group simplification. The existing values shifting rules as they apply to groups of companies were identified as being particularly complex and uncertain in effect, leading to additional compliance costs.

Degrouping charges

Draft legislation

SCHEDULE 1 Section {j1315}

CORPORATE CAPITAL GAINS: COMPANY CEASING TO BE MEMBER OF GROUP [J1315S]

Degrouping

1 In section 171A of TCGA 1992 (election to reallocate gain or loss to another member of the group), omit subsection (7).

2 (1) Section 179 of TCGA 1992 (company ceasing to be member of group) is amended as follows.

(2) In subsection (1)(a) for "company B is a member of a group" substitute "company A and company B are members of the same group".

(3) In subsection (1A) omit the words from "For this purpose" to the end.

(4) For subsection (2) substitute—

"(2) Where 2 companies cease to be members of the group at the same time, subsection (1) does not have effect as respects the acquisition of an asset by one of the companies from the other if condition A or B is met.

(2ZA) Condition A is that the companies—

(a) are both 75 per cent subsidiaries and effective 51 per cent subsidiaries of another company on the date of the acquisition, and

(b) remain both 75 per cent subsidiaries and effective 51 per cent subsidiaries of that other company until after they cease to be members of the group.

(2ZB) Condition B is that one of the companies—

(a) is both a 75 per cent subsidiary and an effective 51 per cent subsidiary of the other on the date of the acquisition, and

(b) remains both a 75 per cent subsidiary and an effective 51 per cent subsidiary of the other until after the companies cease to be members of the group."

(5) For subsection (2A)(a) substitute—

"(a) a company ("company A") acquired an asset from another company ("company B") at a time when both company A and company B were members of the same group ("the first group"),

(aa) company A has ceased to be a member of the first group,".

(6) After subsection (3) insert—

"(3A) Any chargeable gain or allowable loss which would otherwise accrue to company A on the sale referred to in subsection (3) does not so accrue if—

(a) company A ceases to be a member of the group in consequence of—

(i) a disposal of shares in company A or another member of the group made by a member of the group, or

(ii) two or more such disposals, and

(b) subsection (3B) applies to the disposal or, if there is more than one disposal, to at least one of them.

(3B) This subsection applies to a disposal of shares if—

(a) the company making the disposal is resident in the United Kingdom at the time of the disposal, or

(b) the shares are chargeable assets in relation to that company immediately before that time.

In this section "group disposal" means a disposal within subsection (3A)(a) to which this subsection applies.

(3C) If subsection (3A) applies, any chargeable gain or allowable loss accruing to a company ("the transferor company") on a group disposal is to be calculated—

(a) where a chargeable gain would accrue to company A in the absence of subsection (3A), as if the amount of the consideration for the group disposal were increased by the amount of the gain, and

(b) where an allowable loss would accrue to company A in the absence of subsection (3A), as if an amount equal to the amount of the loss were a sum allowable under section 38 as a deduction in the computation of the gain or loss accruing on the group disposal.

(3D) If there is more than one group disposal, the references in subsection (3C) to the amount of the gain or loss are to be read, in relation to each disposal, as references to—

(a) such proportion of that amount as the transferor companies in relation to the group disposals jointly elect as the appropriate proportion in relation to the disposal in question, or

(b) if no election is made, the proportion of that amount attributable to that disposal if that amount is divided equally between the group disposals.

(3E) An election under subsection (3D) must—

(a) specify the appropriate proportion in relation to each group disposal, and

(b) be made, by notice to an officer of Revenue and Customs, no later than 2 years after the end of the first accounting period of a company in which any chargeable gain or allowable loss on a group disposal accrues.

(3F) If a group disposal by a company consists of shares of more than one class, then, for the purposes of subsection (3C), that company may apportion any increase or deduction to be made between the classes of shares in such manner as it considers appropriate."

(7) For subsection (5) substitute—

"(5) Subsections (6) to (8) apply where—

(a) in the absence of subsection (6), company A would be treated by virtue of subsection (3) as selling an asset at any time, by reason of ceasing to be a member of the group, and

(b) company A ceases to be a member of the group by reason only of the fact that the principal company of that group becomes a member of another group.”

(8) In subsection (6)—

(a) for “The company” to “but” substitute “Subsection (3) does not apply to treat company A as selling the asset at that time; but”, and

(b) for “the company in question” (in each place) substitute “company A”.

(9) In subsection (7) for “the company” (in both places) substitute “company A”.

(10) After that subsection insert—

“(7A) Any chargeable gain or allowable loss which would otherwise accrue to company A on the sale referred to in subsection (6) does not so accrue if—

(a) company A ceases at the relevant time to satisfy the conditions in subsection (7) in consequence of—

(i) a disposal of shares in company A, or another member of the other group mentioned in subsection (5), made by a member of that other group, or

(ii) two or more such disposals, and

(b) subsection (3B) applies to the disposal or, if there is more than one disposal, to at least one of them.

(7B) Where subsection (7A) applies, subsections (3C) to (3F) apply to the calculation of any chargeable gain or allowable loss accruing on a disposal within subsection (7A)(a) to which subsection (3B) applies (a “relevant disposal”) with the following modifications—

(a) in subsections (3C) to (3F) for the references to a group disposal substitute references to a relevant disposal, and

(b) in subsection (3C) for the references to subsection (3A) substitute references to subsection (7A).”

(11) In subsection (8) for the words from “the company” to the end substitute “company A on the sale referred to in subsection (6) is to be treated as accruing immediately before the relevant time.”

(12) In subsection (10), for paragraph (a) substitute—

“(a) 2 companies are associated with each other if one is a 75 per cent subsidiary of the other or both are 75 per cent subsidiaries of another company.”

(13) After that subsection insert—

“(10A) For the purposes of this section an asset is a “chargeable asset” in relation to a company at any time if any gain accruing to the company on a disposal of the asset by the company at that time would be a chargeable gain and would by virtue of section 10B form part of its chargeable profits for corporation tax purposes.”

3 After section 179 of TCGA 1992 insert—

“179ZA Claim for adjustment of calculations under section 179

(1) This section applies where a gain accrues to a company (“company A”) on a sale referred to in subsection (3) or (6) of section 179.

(2) If subsection (3C) of that section applies in relation to one or more disposals of shares—

(a) the company making the disposal, or

(b) if there is more than one disposal, the companies making those disposals acting jointly,

may make a claim for the amount of the gain to be treated for the purposes of that subsection as reduced by an amount specified in the claim.

(3) In any other case, company A may make a claim for the amount of the gain to be treated for all purposes of this Act as reduced by an amount specified in the claim.

(4) Where a claim is made under subsection (2) or (3), the gain must be treated, for the purposes mentioned in the subsection in question, as reduced by such amount (if any) as is just and reasonable having regard to the matters mentioned in subsection (5).

(5) Those matters are—

(a) the amount of share capital of company A or any associated company, and

(b) any transaction as a direct or indirect result of which company A or any associated company acquired the asset to which the gain relates.

(6) Where under this section the gain accruing to company A on a sale referred to in subsection (3) or (6) of section 179 is treated as reduced by an amount ("the permitted deduction"), the subsection in question has effect, so far as it provides for the immediate reacquisition of the asset by company A, as if the reference to market value of the asset were to its market value less the permitted deduction."

4 In TCGA 1992, omit—

(a) section 179A (reallocation within group of gain or loss accruing under section 179),

(b) section 179B (roll-over of degrouping charge on business assets), and

(c) Schedule 7AB (roll-over of degrouping charge: modification of enactments).

Substantial shareholding exemption

5 (1) Schedule 7AC to TCGA 1992 (exemptions for disposals by companies with substantial shareholdings) is amended as follows.

(2) After paragraph 15 insert—

"Effect of transfer of trading assets within a group

15A (1) For the purposes of this Part, the period for which the investing company is treated as holding a substantial shareholding in the company invested in is extended in accordance with sub-paragraph (3) if the following conditions are met.

(2) The conditions are—

(a) that, immediately before the disposal, the investing company holds a substantial shareholding in the company invested in,

(b) that an asset which, at the time of the disposal, is being used for the purposes of a trade carried on by the company invested in was transferred to it by the investing company or another company,

(c) that, at the time of the transfer of the asset, the company invested in, the investing company and, if different, the company which transferred the asset were all members of the same group, and

(d) that the asset was previously used by a member of the group (other than the company invested in) for the purposes of a trade carried on by that member at a time when it was such a member.

(3) The investing company is to be treated as having held the substantial shareholding at any time during the final 12 month period when the asset was used as mentioned in sub-paragraph (2)(d) (if it did not hold a substantial shareholding at that time).

(4) "The final 12 month period" means the period of 12 months ending with the time of the disposal."

(3) In paragraph 19 (requirements relating to the company invested in), after sub-paragraph (2) insert—

"(2A) If the conditions in paragraph 15A(2)(b) to (d) are met, sub-paragraph (2B) applies for the purpose of determining whether the requirement of sub-paragraph (1)(a) is satisfied.

(2B) The company invested in is to be treated as having been a trading company at any time during the final 12 month period when the asset was used as mentioned in paragraph 15A(2)(d) (if it was not a trading company at that time).

(2C) "The final 12 month period" has the meaning given in paragraph 15A(4)."

Intangible fixed assets: degrouping

6 (1) Part 8 of CTA Act 2009 (intangible fixed assets) is amended as follows.

(2) In section 780 (deemed realisation and reacquisition at market value), in subsection (5)(b) before "associated" insert "certain".

(3) In section 783 (associated companies leaving group at same time), for subsection (1) substitute—

"(1) Where two companies cease to be members of a group at the same time, section 780 does not apply in relation to a transfer by one of the companies to the other if condition A or B is met.

(1A) Condition A is that the companies—

(a) are both 75% subsidiaries and effective 51% subsidiaries of another company on the date of the transfer, and

(b) remain both 75% subsidiaries and effective 51% subsidiaries of that other company until after they cease to be members of the group.

(2) Condition B is that one of the companies—

(a) is both a 75% subsidiary and an effective 51% subsidiary of the other on the date of the transfer, and

(b) remains both a 75% subsidiary and an effective 51% subsidiary of the other until after the companies cease to be members of the group.",

and, in the section heading, for "*Associated*" substitute "*Certain associated*".

(4) In section 788 (provisions supplementing provisions about degrouping), for subsection (3) substitute—

"(3) For the purposes of those sections and this section two companies are associated with each other if one is a 75% subsidiary of the other or both are 75% subsidiaries of another company."

Consequential repeals

7 In consequence of the omissions made by paragraph 4, omit—

(a) in IHTA 1984, section 97(1)(a)(iii) and "or" before it,

(b) in FA 2002, section 42(1) and (3)(a),

(c) in F(No.2)A 2005, in Schedule 4, paragraphs 8 and 10(3), and

(d) in FA 2009, in Schedule 12, paragraph 2.

Commencement

8 (1) The amendments made by paragraphs 1 to 4 and 7 have effect in relation to any disposal of an asset by one company to another company ("the transferee company") at a time when both companies are members of the same group, if—

(a) the transferee company ceases to be a member of that group on or after the passing of this Act, or

(b) where the transferee company ceased to be such a member before the passing of this Act in circumstances where section 179(6) to (8) applied, the transferee company ceases to satisfy the conditions in section 179(7) on or after the passing of this Act.

(2) The amendments made by paragraph 6 have effect in relation to any disposal of an asset by one company to another company ("the transferee company") at a time when both companies are members of the same group, if—

(a) the transferee company ceases to be a member of that group on or after the passing of this Act, or

(b) where the transferee company ceased to be such a member before the passing of this Act in circumstances where section 783 of CTA 2009 applied, the transferee company ceases to be a member of another group on or after the passing of this Act.

(3) The amendments made by paragraph 5 have effect in relation to disposals of shares on or after the passing of this Act.

EXPLANATORY NOTE

SCHEDULE [XX]: CORPORATION TAX - SIMPLIFICATION - DEGROUPING CHARGES

SUMMARY

1. Schedule [XX] simplifies certain aspects of the rules for the calculation of degrouping charges in the corporation tax regimes for chargeable gains and intangible fixed assets. The Schedule also addresses interactions between the chargeable gains degrouping charge rules and the exemption for disposals of substantial shareholdings. The changes have effect where companies leave a group on or after the passing of the Act, and in relation to share disposals on or after that date.

DETAILS OF THE SCHEDULE

2. Paragraph 1 removes the provision that otherwise prevents a degrouping charge being subject to an election to transfer any resulting gain or loss to another company in the same group under section 171A of the Taxation of Chargeable Gains Act 1992 ('TCGA'). Previously such transfers were dealt with under section 179A, which is being repealed.

3. Paragraph 2 amends the main degrouping charge provisions at section 179 TCGA.

4. Sub-paragraph (2) ensures that a degrouping charge can only arise in respect of an asset transferred between two companies at a time when both are members of the same group.

5. Sub-paragraph (4) amends the 'associated companies exception' in section 179(2) TCGA, which prevents a degrouping charge arising where two associated companies leave a group together, and an asset has previously been transferred between those associated companies. The new exception applies where two companies are part of the same sub-group at all times from when the asset is transferred until immediately after they leave the original group.

6. Sub-paragraph (6) introduces new rules at section 179(3A) to (3F) TCGA which provide a new mechanism for bringing into account a degrouping charge where it arises on a company leaving a group as a result of a disposal of shares by a group company within the charge to corporation tax. In such cases, any degrouping gain or loss will instead result in an adjustment to the chargeable gain or allowable loss that arises on the share disposal.

7. Subsection (3A) disapplies the normal operation of the degrouping charge in the circumstances mentioned above.

8. Subsection (3B) applies the new mechanism to companies within the charge to corporation tax.

9. Subsection (3C) provides that the degrouping gain or loss will result in an adjustment to the chargeable gain or allowable loss of the group company making a share disposal.

10. Subsection (3D) applies where a company leaves the group as a result of more than one group company making a share disposal. In those circumstances the adjustment will be shared equally or, if they so elect, as the companies wish.

11. Subsection (3E) sets out the requirements for an election under subsection (3D).

12. Subsection (3F) applies where a company leaves a group as a result of a company making a disposal of more than one class of shares. In those circumstances the company may allocate the adjustment between each class of shares as it wishes.

13. Sub-paragraphs (7) to (10) apply the new mechanism to situations where a degrouping charge does not arise immediately at the point a company leaves a group, but only where certain other conditions are no longer met.

14. Sub-paragraph (11) changes the time a degrouping charge accrues in cases where a company leaves a group (other than through a disposal of shares) where that charge arises because a condition is no longer met. This change is to allow the procedure for transferring gains and losses in groups in section 171A TCGA to apply.

15. Sub-paragraph (12) defines "associated companies" for the purposes of section 179(3) TCGA. This reflects the changes made to the exception to the charge in section 179(2).

16. Sub-paragraph (13) provides a definition of "chargeable asset" for the purposes of the section as a whole. This was previously in section 179(1A) TCGA.

17. Paragraph 3 provides a new procedure for claiming a reduction in a degrouping charge set out in new section 179ZA TCGA.

18. New subsection (2) allows a claim to be made for the reduction of the amount by which a degrouping charge is taken into account in calculating a gain on a disposal of shares under section 179(3C) TCGA.

19. New subsection (3) allows a similar claim in the case of a charge that arises on a deemed sale under section 179(3) on the company leaving the group.

20. New subsection (4) provides that the effect of the claim is that the gain is reduced by an amount that is just and reasonable.

21. New subsection (5) sets out the factors to be considered when making an adjustment: the amount of share capital of the company leaving the group and the transactions by which it acquired the asset.

22. New subsection (6) ensures that any reduction in the gain as a result of a claim is reflected in the cost of the asset for tax purposes.

23. Paragraph 5(1) introduces amendments to the Substantial Shareholding Exemption in Schedule 7AC TCGA that will allow the exemption to apply in situations involving the disposal of part of a group's trading activity that has been transferred to a new company.

24. Sub-paragraph (2) introduces a new paragraph 15A into Schedule 7AC which treats the minimum 12 month substantial shareholding requirement as having been met for the period that assets were used for a trade conducted by the group before being transferred to the company being disposed of.

25. Sub-paragraph (3) amends paragraph 19 of Schedule 7AC. Where the new paragraph 15A applies the company being disposed of may be treated as having been a trading company for periods within the 12 months prior to the disposal. This applies where it was not a trading company at the time but the assets transferred to it were used for the purposes of the trade the company carried on at the time of the disposal.

26. Paragraph (6) amends the exception to the degrouping charge under the Intangible Fixed Assets rules in line with the changes to the capital gains at paragraph 2(4) of the Schedule.

27. Paragraph (7) is the commencement provision. The changes to the degrouping charge will apply to companies leaving groups on or after the passing of the Act. Changes to the Substantial Shareholding Exemption have effect in relation to disposals of shares on or after that date.

BACKGROUND NOTE

28. The changes introduced by this clause are one of the results of a consultation process run by HM Treasury and HMRC aimed at simplifying the group aspects of the corporation tax chargeable gains regime.

29. The Government issued a discussion document in July 2009, outlining options for change in this and other areas, and followed with a consultation document in February 2010, including draft legislation on which this clause is based.

C Summary of responses to discussion document

List of respondents

The Government is grateful to all those who have contributed to the consultation process. The following companies and representative bodies submitted written responses to the discussion document:

Amcor Europe Group Management

AstraZeneca UK Limited

BP plc

British Sky Broadcasting Ltd

Caterpillar European Tax Services

Confederation of British Industry

The Chartered Institute of Taxation

The City of London Law Society

Deloitte LLP

Institute of Chartered Accountants in England and Wales

Institute of Chartered Accountants of Scotland

Institute of Directors

KPMG LLP

The Law Society

Linklaters LLP

Lloyds Banking Group

London Society of Chartered Accountants

PKF (UK) LLP

Powrie Appleby LLP

PricewaterhouseCoopers LLP

United Kingdom Oil Industry Taxation Committee

Capital losses after a change in ownership

The discussion document included the following options:

3A Repeal only those parts of Schedule 7A that are no longer required following the introduction of the second TAAR (section 184D, TCGA).

3B Align the change of ownership rules retained within Schedule 7A with the approach of the second TAAR.

3C Repeal the loss buying rules in Schedule 7A and introduce in their place a permissive rule that allows realised capital losses to be carried forward without restriction in cases where the losses relate to a trade or business that continues in a recognisable form.

3D Repeal the loss buying rules in Schedule 7A without replacement.

Overview of comments received

- There was a widespread view among respondents that 3D would be the most desirable option, but many appreciated that this might not be possible given fiscal constraints.
- On this basis, many respondents supported some combination of 3B and 3C and stated that this would improve certainty for taxpayers.
- A number of stakeholders felt that the lead option (i.e. some combination of 3B and 3C) would also achieve an admin burden reduction.
- Several stakeholders commented that they welcomed the reference to "trade or business" in option 3C.
- Several stakeholders stressed that care would need to be taken with the lead option to ensure that the new provisions did not impact on commercial transactions.
- Very few suggestions on alternative routes to simplification were received. One suggestion that was received was to introduce a de minimis limit for streaming.

Value shifting and depreciatory transactions

The discussion document included the following options:

4A Simply to extend the existing depreciatory transaction rules to allow for adjustment to gains on shares (including the creation of a gain); or

4B Retain the existing depreciatory transaction legislation and create a new value shifting rule within the chapter of TCGA dealing with groups of companies[10] which would be effect based as in the present depreciatory transactions rules.

4C In addition to the above, to align the time limit for adjustments between the two sets of rules, to six years (to match the present provision in section 31).

Overview of comments

- Respondents generally agreed that simplification of the areas of the value shifting and depreciatory transactions legislation would be helpful.

[10] Part VI, Chapter 1 TCGA

- There was support for a principles-based rule among a number of stakeholders, though others warned that such a rule had the potential to reduce certainty for taxpayers, especially those already familiar with the existing value-shifting provisions.
- Respondents were divided over whether 4A or 4B would be the better approach.
- Most respondents supported option 4C, or a shorter time limit.

Degrouping charges

The discussion document included the following options:

5A Introduce a facility to make a just and reasonable adjustment to the degrouping charge through a taxpayer election where the present rules give a result that does not reflect a true economic profit.

5B Introduce a mechanism to switch off the degrouping charge where the whole gain is realised at the shareholder level, to replace the exceptions in the present section 179(2) TCGA.

5C Leave the degrouping charge as it stands, but look for a means to adjust the base cost of the shares in the company being sold, so that together the degrouping charge and any gain or loss on the share sale reflect the true economic profit from the whole transaction, and thereby eliminate any excess degrouping charge.

5D Amend the degrouping charge rules so that any charge will arise either in the transferor company or the group's principal UK company, providing for elections to subsidiaries if necessary.

5E Reduce the six year limit in the degrouping charge rules to three years.

5F Replace the current de-grouping charge with a principle based TAAR.

5G The degrouping charges rules could be disapplied in respect of trade assets where a disposal of shares in a group company qualifies for the exemption under SSE.

Overview of comments

- The majority of respondents supported option 5A, though several added that they thought its benefit would largely be to remove double taxation, rather than to decrease admin or compliance burdens.
- There was a mixture of views on whether option 5D would reduce compliance burdens. However, more respondents supported the option (feeling it would reduce burdens) than were actively against it. 5D received support largely from business rather than from professional services firms.
- A large majority of respondents were keen to see 5G introduced.
- Several respondents said that for 5G to meet its aim fully, it should include an easing of the SSE requirements to allow the sale of a trade that a group has been continuing for over 12 months even if the vehicle entity has not been in place for over 12 months.

- Some respondents observed that the interaction of 5G with intangibles provisions, loan relationship assets rules and derivative contract assets rules would need to be considered.

- Only a few respondents thought that 5G could lead to abuse. One suggestion was that, as framed in the discussion document, the option could allow groups to "swamp" investment assets with trading assets in a subsidiary that met the SSE conditions, and hence remove any degrouping charge.
- A few respondents said that reform of the degrouping charge rules could be a good opportunity for the HMRC guidance on the meaning of "associated companies" for the purposes of s179(2) TCGA (issued following the *Johnston Publishing* decision)[11] to be put into legislation.

[11] Johnston Publishing (North) Ltd v Revenue and Customs Commissioners [2008] EWCA Civ 858; [2008] WLR (D) 253

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