

BREAKING UP & STAMPING

It is never an easy task to provide tax advice to clients who are about to divorce, but this unease is compounded when it dawns on the client that not only will he or she be obliged to share assets with an estranged spouse but may also be required to pay a share to H M Revenue & Customs.

In many instances, all that the parties are seeking to achieve is a simple exchange of marital assets, and we are all aware that the tax advice will differ depending on how early in the marriage breakdown the advice has been sought.

Take the couple who ceased to live together in the previous tax year and are now divorcing and wish to split up the trading company that they had built up together and in which they each held 50% of the equity. The company operates two residential nursing home businesses that are broadly of equal value and they have agreed to each take a nursing home and its associated business and go their separate ways. The harshness of the capital gains tax regime can be overcome by carrying out an 'exempt demerger' which will also exempt the distribution of company property from income tax.

But that isn't the end of the story. The splitting of the company will also involve the transfer of fairly valuable properties, one of which is valued at £2.25m and the other at £2.75m so that SDLT is relevant. This transaction fails to qualify for Reconstruction Relief which provides full exemption as it is not what is often termed a 'cross the board' demerger but will qualify for Acquisition Relief which limits the SDLT charge from the full rate of 4% to a rate of ½%.

There are two ways in which the transaction may be carried out. If the parties are content for one of the two Residential Home trades to be transferred to a new company which will be controlled by one spouse leaving the other spouse in control of the existing company and its remaining residential home and trade, SDLT of ½% will be chargeable on the value of the property transferred. Sensibly, the property with the lower value would be demerged and SDLT of £11,250 is payable on the transfer to the new company of the property valued at £2.25m.

But what if neither spouse is prepared to inherit the "baggage" of the existing company, and both wish to carry on their respective trade from a newly incorporated company. In this case, in addition to the legal costs of winding up the company, SDLT of £25,000 would be payable on property worth £5m.

And don't forget, the SDLT relief might unravel so that the full rate would become payable if the ownership of the company to which the demerged trade has been transferred changes within three years whilst the company still owns the transferred property.

About the author ...

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*Page 2 - for Q&A's this month from Tax Panel member
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Page 3 - for Tax Panel members and their specialisms

UK200Group Talking Tax Q & As – April 2012

Members of our Tax Panel each month look at issues they have come across and share these with members and readers of UK200Group's Talking Tax.

This month's Q & As supplied by Chris Mattos of Randall & Payne LLP

“Excluded activities”

Q Is this something to do with EIS?

A Yes - and the same legislation (ITA 2007, s189(1)), applies to VCT and will apply for Seed EIS

Q Are these the same as those relating to EMI?

A Yes and no! – the items listed are the same for each scheme but the legislation for EMI can be found at ITEPA 2003, Sch 5, Para 16

Q So a company doesn't qualify for these schemes if it carries on these activities?

A Not quite, it's a wholly or substantially test, so it is possible for a company to carry some of these activities

Q What are the excluded activities?

A See below:

- dealing in land, in commodities or futures or in shares, securities or other financial instruments;
- dealing in goods otherwise than in the course of an ordinary trade of wholesale or retail distribution;
- banking, insurance, money-lending, debt-factoring, hire-purchase financing or other financial activities;
- leasing, including letting ships on charter or other assets on hire;
- receiving royalties or licence fees;
- providing legal or accountancy services;
- property development;
- farming or market gardening;
- forestry activities and timber production;
- shipbuilding, coal and steel production;
- operating or managing hotels or comparable establishments, or property used as such;
- operating or managing nursing or residential care homes, or property used as such;
- providing services or facilities for any trade carried on by another person which consists to any substantial extent of the above activities.

Q There seem to be some very wide definitions - how do I know if HMRC will deem an activity as excluded?

A Ask them! The Small Company Enterprise Centre are very helpful and you can usually speak to a knowledgeable Inspector straight away – their number is 0115 974 1250.

Q Doesn't look good for farmers though...

A That's what I always thought but it goes to make the wholly and substantially test. I've heard recent cases that Champagne production (on 70 acres of land growing the grapes) and specialist cheese production (on a dairy farm) were both allowed for EIS as the main activity in both cases centred around production

Q Could my client's B&B qualify as I don't think that is a hotel?

A Whilst there is no definition of a hotel, the legislation defines a 'comparable establishment' to an hotel as including a guest house, hostel or other establishment the main purpose of which is the provision of facilities for overnight accommodation

Q What about our management services company we have that supplies services to our accounting practice?

A Not likely! The question is what are the services provided, in most cases these are accounting services provided to the practice who in turn invoice the client. See *Castleton Management Services Ltd v Kirkwood (2001)*

Other management companies should be OK, and I have had previous agreement from HMRC re management and HR consultancies that they should be okay too.

For further information on any of the above ...

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UK200Group Tax Panel members are renowned for their depth of knowledge and can advise on all areas of taxation with special expertise and experience of multinationals, UK companies, privately-owned organisations, sole traders, family businesses, trusts, partnerships and private individuals. Straight forward general enquiries will be dealt with quickly and free of charge. More complex specific client enquiries may require a fee charge which will be discussed and agreed by both parties prior to any work being undertaken. Tax enquiries can be posted to www.uk200group.co.uk members' home page under Specialist Panels, Tax Panel Newsgroup. The Centre is alerted to all enquiries posted on the UK200Group web site.

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|--|--------------------------------|--|--------------------------|
| 1 Capital Gains Tax | 2 Sales & Acquisitions | 3 Employee Share Incentives | 4 Inheritance Tax |
| 5 International Tax | 6 Offshore Tax Planning | 7 Partnership Tax Planning | 8 PAYE and NI |
| 9 Stamp Duty Land Tax | 10 Tax Investigations | 11 Taxation of Owner Managed Businesses | 12 Trusts |
| 13 UK Taxation of Foreign Expatriates | | 14 VAT | |

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