



Chartered  
Institute of  
Taxation

30 Monck Street  
London SW1P 2AP  
T: +44 (0)20 7340 0550  
E: [post@ciot.org.uk](mailto:post@ciot.org.uk)

## Budget 2021 Representations: changes to the tax rules effecting companies

By the Chartered Institute of Taxation

### 1 Executive Summary

- 1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.
- 1.2 We believe that the tax system can offer support to businesses as the UK emerges from the pandemic and seeks to build a strong economic recovery. We suggest the following measures are considered for the Spring Budget which we think could promote recovery and growth:
- **Corporate tax losses:** follow the precedent set in the difficult times of about 30 years ago, and allow a three year carry back of business tax losses arising over the period of the COVID epidemic and consider relaxing the rules around the recently introduced 50% loss relief restrictions.
  - **Capital allowances:** set the level of the annual investment allowance (AIA) on a permanent basis, we suggest at £1million pa. This will create certainty for businesses contemplating investment projects and avoid arbitrary cliff edges around dates, sometimes announced late in the day, that have been a too common occurrence over recent years due to fluctuations in the level of the AIA. Additionally it will send the message that the government recognises the overall benefit of capital expenditure and investment by businesses.
  - **Rules which apply on changes in ownership of businesses:** clarify what will constitute a major change in the nature or conduct of a trade carried on by a company to reflect the circumstances that have arisen as a result of COVID-19.
  - **Re-organisations of businesses more generally:** ensure relief from stamp duty for all partition demergers; consult on simplifying the rules relating to re-organisations of businesses to help businesses which may wish to reorganise, diversify or merge, particularly as a result of changes to their businesses due to COVID-19; and improve the facility to obtain clearances.
  - **UK to UK transfer pricing:** an opportunity arises following the UK leaving the EU for tax measures that were introduced solely to ensure the UK law complied with the then understanding of EU law to be repealed. UK to UK transfer pricing is one such measure that warrants consideration for repeal.

## **2 About us**

- 2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 2.2 The CIOT’s work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.
- 2.3 The CIOT draws on our members’ experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.
- 2.4 Our members have the practising title of ‘Chartered Tax Adviser’ and the designatory letters ‘CTA’, to represent the leading tax qualification.

## **3 Introduction**

- 3.1 CIOT commends the government on the action it has taken to date to support businesses through the COVID-19 pandemic, including the Coronavirus Job Retention Scheme (CJRS), the Self-Employment Income Support Scheme (SEISS) and the various business loan schemes. But we believe that the tax system can also offer support to businesses as we emerge from the pandemic and seek to build a strong economic recovery. We set out below some suggestions for changes to the tax rules which we think could promote recovery and growth. We would be happy to discuss these suggestions with ministers or officials.
- 3.2 Our objectives for the tax system include a legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences, and greater certainty, so businesses and individuals can plan ahead with confidence. The measures proposed would support these aims.
- 3.3 We recognise that some of the measures we propose would have a cost to the Exchequer which will have to be considered and balanced with their ability to help businesses through the economic downturn and to maximise growth as we come out of it.
- 3.4 The intention is that the measures proposed below would give businesses improved cash flow and, therefore, assist them to invest, and take other actions, which may be necessary to ensure that businesses survive the difficult times ahead as confidence returns and the economy recovers.
- 3.5 We recognise that it is difficult to devise corporation tax measures that target businesses most affected by the pandemic, without also reducing the corporation tax burden for companies more generally, although, as indicated below, some of the measures can be focused on losses or events arising from the pandemic. The measures suggested have arisen from discussions with our members who advise businesses and are where the members consider that changes to the rules would provide the most effectively targeted assistance to businesses.

#### 4 Corporate tax losses

##### 4.1 **Proposal: Allow a three year carry back of business tax losses arising over the period of the COVID epidemic and consider relaxing the rules around the recently introduced 50% loss relief restrictions.**

4.2 Our proposal to allow a three year carry back of business tax losses arising over the period of the COVID epidemic would give businesses which have a track record of making profits and paying tax, but which have suffered over the last year, a much-needed cash injection. In many cases (where the business would ultimately have recovered in any event), it will be a cash flow cost to the government which will reverse as the company, having used up its losses by carrying them back, makes profits and pays tax sooner in the future. For businesses that would not have survived but for the ability to utilise these losses early, there will be a cost to the government in giving value for these losses, as if the business had indeed failed the losses would have lapsed. But we suggest that in these circumstances, allowing the losses to be carried back and thereby 'encashed' will be money well spent, in that it will have saved the business. Other taxes will continue to be paid, and income or corporation taxes will be paid as profits return. We accept that a few businesses may make use of the carry back and go on to fail anyway, but this measure will have given these businesses the best possible chance of success. Overall, we think that this targeted measure now makes good sense, even if ultimately there is a need for fiscal consolidation.

##### 4.3 Trading losses

Consideration should be given to permitting more flexibility around the use of trading losses for all businesses, companies and sole traders and partnerships. In particular, the government should consider allowing (perhaps for a time limited period) the extended carry back of trading losses for up to three years in all circumstances (rather than only on the cessation of a trade).

4.4 The additional flexibility could be focussed on losses arising as a result of the pandemic by, for instance, limiting the extended carry back to trading losses arising in accounting periods overlapping, say, the year from 1 March 2020. This would offer a cash flow benefit to those businesses incurring losses as a result of the pandemic.

4.5 Permitting an extended carry back of losses would also be a measure focussed on businesses with a longer recent track record of profitability. We accept that that is not the same as future viability, but it may be one of the best proxies available.

##### 4.6 Corporation tax losses – 50% restriction

We also suggest that the government should give consideration to relaxing the rules around the 50% restriction on loss relief for companies in respect of both income losses and capital losses, so that all companies can fully utilise losses arising as a result of the detrimental effect of the pandemic.

##### 4.7 Cost to the Exchequer

With regard to cost to the Exchequer, we note that the cost of the carry back proposal would reverse out when businesses start to make a profit in the future (as they will begin to pay tax again without the losses that would otherwise have been available to be carried forward). In addition, we would expect that the immediate cost of the loss relief is less than the costs which arise for the economy as a whole if businesses fail.

#### 4.8 Precedent

There is precedent for measures such as these in times of severe financial economic downturns. Such measures were taken in the recession around 1990 and, again (though on a more limited basis), in 2009 in response to the financial crash of 2008.

### 5 **Capital allowances**

#### 5.1 **Proposal: Set the Annual Investment Allowance (AIA) at £1 million on a more permanent basis.**

5.2 The current AIA level of £1million was a temporary increase (from the AIA limit of £200,000) for two calendar years 2019 and 2020. It has been extended for another year, by an announcement in November 2020.

5.3 Setting the AIA at a level of £1million ensures that the majority of businesses continue to achieve 100% relief for their capital expenditure on qualifying plant and machinery for the immediate future at a time when encouraging businesses to continue to invest in plant and machinery will be especially important to support the recovery of the economy.

5.4 A consistent level of AIA will also avoid the cliff edges that have been a too common occurrence over recent years due to fluctuations in the AIA level.

#### 5.5 Costs to the Exchequer

The CIOT believes there has been too much tinkering with rules and rates of capital allowances. In our view such frequent change more often than not brings complexity and uncertainty, and undermines investor understanding of, and confidence in, what is on offer at any one time. Most businesses cite certainty as more important than the precise amount of relief available. Putting the AIA on a more permanent footing would boost investor and business confidence at relatively modest cost to the Exchequer.

### 6 **Changes in ownership**

#### 6.1 **Proposal: HMRC should clarify what will constitute a major change in the nature of conduct of a trade carried on by a company which may otherwise restrict the availability of losses to businesses which change ownership to reflect the circumstances that have arisen as a result of COVID-19.**

6.2 There are rules in the corporation tax code which prevent the use of trading losses going forward in certain circumstances following a change in a company's ownership<sup>1</sup>. Broadly, there is a restriction in the relief available in respect of trading losses where within any period of five years (three years for periods before 1 April 2017) there is both (a) a change in the ownership of a company and (b) a major change in the nature or conduct of a trade carried on by the company.

6.3 We envisage that there could be a significant amount of both changes in the nature or conduct of trades and changes in ownership as a result of the COVID-19 pandemic, as businesses work out new ways of operating or diversify and/or merge in order to remain viable. It has often been difficult in practice to determine whether

---

<sup>1</sup> CTA 2010 Part 14 Change in company ownership

there has been a major change in the nature or conduct of a trade, so as to be caught by the rules referred to above, and we suggest that consideration should be given to providing some assistance in this area.

- 6.4 One way to achieve this would be to indicate that there should be a 'light touch' around what constitutes a major change. For example, this could be done through guidance or statements of practice setting out that, for example, changes by pubs and restaurants to become takeaway outfits, or even corner shops, are not a major change in the nature of their trade. In this regard, we note that HMRC has recently updated its guidance on crisis-driven changes to trading activities - [BIM48000](#). Whilst this offers some guidance in this area, it is predominantly focussed on commencement and cessation of trades, so it is not directly on point. However, this guidance could be built on and broadened to also consider major changes to a trade.
- 6.5 Alternatively, a clearance procedure could be introduced to confirm whether or not there has been a major change, although we appreciate that this would only be of assistance with regard to changes that have occurred before the change in ownership (the rules apply if the relevant change occurs in the relevant period, whether before or after the change in ownership transaction). Consideration could also be given to legislating to ensure that the rules will not apply for a period if a change of ownership and/or nature of a trade of business was materially occasioned by COVID-19 or it occurred in a particular time period, say, between 1 April 2020 and 31 March 2021 (although this date may need to be later if the current restrictions on businesses remain in place).
- 6.6 A relaxation of the current rules in this area would generally facilitate commercial merger and acquisition transactions which may keep companies (and their businesses) alive, which would benefit the wider economy. It would permit a company to continue to use its losses going forward and not be prevented from doing so as a result of a change to its trade brought about by the COVID-19 pandemic. The continued availability of the losses may encourage transactions – changes in ownership – which save the business and which would otherwise not happen, and in the best case scenario mean that the employees keep their jobs.
- 6.7 Cost to the Exchequer

We recognise that this measure would be targeting historic losses and not (or not only) losses arising as a result of the pandemic. In order to ensure that the measure does help promote continuing trades, and benefit the economy by maintaining jobs etc, it may be necessary to impose some conditionality around the 'new' trade; for example that it retains the employees (or a significant number of them). However, in general enabling businesses to utilise tax losses will give them a much-needed cash injection at this difficult time and may ensure their survival. We would expect that the immediate cost of ensuring that businesses can use losses where that might not otherwise have been the case is less than the costs which arise for the economy as a whole if businesses fail.

## **7 Reorganisations**

- 7.1 **Proposal: Ensure relief from stamp duty for all partition demergers; consult on simplifying the rules relating to re-organisations of businesses to help businesses which may wish to reorganise, diversify or merge; and improve the facility to obtain clearance.**
- 7.2 There are a number of areas where the existing rules and tax reliefs for schemes of reconstruction present problems for businesses and often cause transactions to be made unnecessarily complicated in order to ensure that the reorganisation can meet the requirements of the various tax reliefs, so that unexpected tax charges do not arise. We suggest that this period of economic difficulty is an opportune time to consider amending or

updating some of these rules in order to make them easier to operate for corporate businesses and their owners. Restructuring of businesses is likely to become more prevalent as business struggle to regroup and reorganise in order to put themselves in the best position to recover and grow. Our specific proposals are:

- **Stamp duty:** to broaden the reliefs from stamp duty for reorganisations and reconstructions under FA 1986 sections 75 and 77 to more closely reflect the policy (apparent from other taxes) that such transactions should be tax neutral.
- **Demergers:** to consult on changes to the exempt distributions regime, specifically whether any of the restrictions can be removed, with the aim of simplifying the rules so that demergers of businesses can be done tax neutrally.
- **Clearances:** to amend the rules for obtaining a clearance for reorganisations to address the shortfalls in the legislation which can cause practical problems in commercial transactions.

### 7.3 Stamp duty

7.4 We have previously suggested to HMRC<sup>2</sup> that a discussion around the policy rationale of seeking to impose a stamp duty charge on corporate reconstructions would be useful, in particular to consider the scope and policy intent of the reliefs currently available in respect of stamp duty under FA 1986 sections 75 and 77. There is generally relief from other taxes, such as capital gains tax and corporation tax, which ensure that the transactions are tax neutral. It can also be said that any tax charges that do arise on a corporate reconstruction are generally 'dry' tax charges, in that no cash is generated by the transaction. As such it is a real cost to a business or shareholder. Further, in circumstances where the corporate reconstruction takes place in order to facilitate a sale of the business, there should be a stamp duty or SDRT charge on the subsequent sale, and we would also expect that a new combined tax would apply to a subsequent sale.

7.5 Recent changes to the rules on stamp duty on shares, introduced to combat perceived anti avoidance through arrangements known as 'swamping', have also had the effect of a charge to stamp duty on partition demergers (that did not previously arise). We would like to see the stamp duty relief at FA 1986 section 75 extended so that it applies to all transactions that are schemes of reconstruction for capital gains tax purposes (as defined by Taxation of Chargeable Gains Act 1992 Schedule 5AA), rather than the current more limited application to transactions that fall within the company law definition of reconstructions (determined by the judgment in *Re South African Supply and Cold Storage Ltd* [1904] 2Ch 268 to be a reconstruction which resulted in the substantially the same business being carried on by substantially the same persons).

7.6 A broadening of this relief would allow relief from stamp taxes to be available for partition demergers, as well as for non-partition demergers, and would align the reliefs for stamp duty with the reliefs from capital gains tax and corporation tax. We cannot see any obvious policy reason for the current difference in tax treatment for different taxes, and wonder whether this is the result of stamp duty reliefs not keeping pace with changes to the rules applying to capital gains, rather than a considered policy outcome. More generally, reducing the cost of partition demergers would help businesses which wish to pursue this route and reorganise themselves to maximise future growth. The current situation means that some schemes of reconstruction cannot be carried out or have to be carried out in a different way, in order to obtain stamp duty relief or to otherwise mitigate the stamp duty liability.

7.7 We would also welcome some relaxation of the relief at FA 1986 section 77. This relief only applies if the shareholders of the acquiring company hold shares of the same classes and in the same proportions, or as nearly as possible in the same proportions, as their shareholdings in the target company. This means that the

---

<sup>2</sup> In our [CIOT response to Modernisation of STS framework Call for Evidence](#) in October 2020 (see at paragraph 6.6-6.13)

relief is quite restrictive and only applies to quite a narrow range of transactions. We suggest that this relief could reasonably be extended and still give effect to the policy intent of the relief. For example, it is not clear why the acquiring company has to have shares of the same classes as the target company; we suggest that a requirement for ordinary shares would be sufficient. Similarly, the exact 'mirror image' of shareholders is restrictive; we suggest that requiring a commonality of ownership (based on a significant percentage, but less than 100%) could be considered.

7.8 Another area that would benefit from reconsideration is the scope of the rule at FA 1986 section 77A. We recognise that this rule was introduced to counter perceived avoidance in this area, and we support that aim. However, notwithstanding the amendments to the rules that have been made since it was introduced, it still operates unfairly and arbitrarily in some circumstances, resulting in double taxation in relatively simple transactions where there is no avoidance motive; for example, stamp duty may be chargeable, depending on whether a purchaser has been identified before a pre-sale reorganisation takes place.

#### 7.9 Cost to the Exchequer

We recognise that there would be a cost to the Exchequer of providing stamp duty relief in a wider set of circumstances, however the relief will also have a positive effect on the ability of business owners to carry out commercially desirable transactions.

#### 7.10 Demergers

We suggest that the government consults on changes to the exempt distributions regime, specifically whether any of the restrictions can be removed, with the aim of simplifying the rules so that demergers of businesses can be done tax neutrally in the more straightforward way of an exempt distribution, rather than by way of a more complex demerger by reduction of capital or liquidation (in order to ensure that tax charges do not arise). Simplifying the rules will make it easier for businesses to demerge in a tax neutral and cost effective way. Demergers are one of the most complicated areas of tax and transaction structuring. It would be helpful to businesses, particularly in an environment where business demergers and reorganisations might be expected due to the economic shock of COVID-19, if these could be done in the most straightforward way.

7.11 The exempt distributions regime for corporate and group divisions (commonly referred to as 'demergers') is much more restrictive in scope than other available mechanisms. Some of the restrictions were designed to prevent the abuse of distributions and advance corporation tax (ACT) regimes. The ACT regime was repealed by FA 1998 and we suggest that this may be an appropriate time to consider whether all of the restrictions are necessary. We suggest that the regime could be simplified on the basis that the requirements for exempt distribution treatment are aligned with the capital gains tax anti-avoidance rules, that is to say that they are effected for bona fide commercial reasons and do not form part of a scheme or arrangements of which the main purpose, or one of the main purposes, is avoidance of liability to capital gains tax, income tax or corporation tax.

7.12 We recognise that changes to the rules on exempt distributions would be a fairly substantial change to the tax code and, therefore, it would be appropriate for the government to consult on it before deciding on any changes. We are also aware that any demerger that could be carried out using a distribution in specie could also be carried out using a demerger by reduction of capital or by liquidation with (almost) identical tax and economic consequences. The main difference is that these alternatives are more complex and costly to implement. Changes, therefore, should also be considered from a non-tax perspective. Both a liquidation and a capital reduction have safeguards to protect the shareholders and the creditors. These safeguards may be lost if directors are permitted to simply distribute assets to shareholders. Widening the scope of exempt

distributions could be accomplished, but may necessitate some kind of additional protective measures – perhaps a requirement for a solvency statement and special resolution, as required for capital reduction demergers. In other words, non-tax (company) law may need to be updated too. A consultation can explore whether the changes would facilitate completely different behavioural changes or other unintended consequences.

#### 7.13 Cost to the Exchequer

We would expect that any cost to the Exchequer from changes to the exempt distribution regime to be explored as part of the consultation process. However, we would not expect these to be significant because, as noted above, in most cases the demerger can be achieved in another (more complex) way to ensure that tax charges do not arise. The changes to the rules would be intended to ensure that business demergers and reorganisations can be done in the most straightforward way, rather than to significantly impact on whether or not the demergers and reorganisations take place at all.

#### 7.14 Clearances

The facility to obtain a clearance for a range of transactions is extremely useful for taxpayers. However, there are some shortfalls in the legislation dealing with clearances for reorganisations which can cause practical problems in commercial transactions. We suggest amending the rules with regard to clearances as follows:

- permit the clearance applications to be made by any of the shareholders as well as the company.
- permit the clearance application under TCGA 1992 section 139(1) to be made by the transferor company as well as by the transferee company.

7.15 The increased flexibility around who can make a clearance application would be helpful in circumstances where, for example, the company does not wish to make a clearance but one or more of the minority shareholders would like comfort as to their tax position.

7.16 With regard to which company is required to make the clearance application, it is often the case that the transferee company is a new company specifically set up for the purpose. That this is the company which has to make the clearance application results in the costs of setting up this company having to be undertaken before it is certain that the transaction will go ahead. This is an unnecessary cost to businesses and we suggest that it would be a helpful practical amendment to the legislation to permit the clearance application to be made by the transferor company as well as the transferee company.

#### 7.17 Cost to the Exchequer

We would not expect these administrative changes to the availability of clearances to have any Exchequer impact, as the changes will not widen the scope of persons eligible for tax relief. We also think that it is unlikely that the suggested changes would materially impact the number of clearance applications made to BAI Clearance overall, so would not expect that there would be significant resourcing costs either.

## 8 **UK to UK transfer pricing**

### 8.1 **Proposal: Repeal UK to UK transfer pricing.**



8.2 No doubt the government is considering the impact of the UK leaving the EU and the end of the transition period on our tax code. One aspect of the corporation tax rules that merits consideration for repeal is the rules imposing UK to UK transfer pricing. Historically these rules were introduced in response to decisions of the European Court of Justice although subsequently doubt was cast as to the need for them even before Brexit. We would be interested in whether HMRC's information on operation of these rules in practice indicates whether retaining them is worthwhile or required for the integrity of the tax system and if so, what is the reason for that. If not, we would welcome their repeal in order to simplify the corporation tax code for business.

The Chartered Institute of Taxation

13 January 2021