FA2015: entrepreneurs' relief – exclusino of goodwill

OMB Technical

01 June 2015

In the March issue of *Tax Adviser*, we reported that the CIOT had sent comments to HMRC on the draft Finance Bill 2015 clauses concerning the denial of entrepreneurs' relief (ER) for disposals of goodwill to related companies on incorporation.

We had pointed out that the provisions, as originally drafted, could inhibit some commercial transactions, because they would apply whether or not the shareholders of the company were identical to the owners of the previous unincorporated business. We were aware of a case, for example, where a five partner firm was considering incorporating, but two of the partners wished to exit from the firm and be paid out. Our reading of the draft legislation suggested that none of the partners, including the exiting partners, would be able to claim ER on the disposal of goodwill. This is because they would be treated as related parties of the new limited company, by virtue of being associates of the other partners who will become shareholders in the new company (new TCGA 1992 s 169LA (2)). This seemed unreasonable, given that they would no longer have any stake in the business. We said that, in our view, the draft legislation should be amended to make it clear that exiting partners may claim ER.

We are therefore pleased to note that the legislation, which is now in FA 2015 s 42, has been revised to allow ER to be claimed by partners in a firm who do not hold or acquire any stake in the successor company. The concept of a 'retiring partner' is introduced by new TCGA 1992 s 169LA(1)(c). These changes affect transfers on or after 3 December 2014.

This is a sensible revision, removing some potentially unintended consequences from the scope of the legislation.

However, it is not all good news. New TCGA 1992 s 169LA (3) restricts the definition of a ‘retiring partner’ to those who are a related party in relation to the new limited company because they are associated with their former partners; but only because they are partners and not for any other reason. Given that the definition of ‘associate’ in CTA 2010 s 448 is wide, we can foresee that this could exclude genuine retiring partners (particularly family members) from this carve-out to the new legislation. For example, a father and son are in partnership; if the father wants to retire and the son wants to incorporate, it appears that s 169LA (3) will prevent the father qualifying for ER on his retirement.

HMRC have told us that they have defined a ‘retiring partner’ in a concise and fairly narrow sense because they thought it would be more difficult to devise a wider carve-out ‘without risking the reintroduction of the very unfairness the measure is designed
to prevent’.

We understand that HMRC will be updating the CGT manual to reflect all the changes to ER made in FA 2015. The target date for publication is late summer 2015.