

TAXREP 32/01

TREASURY SHARES

Text of a memorandum submitted in November 2001 by the Tax Faculty to the Inland Revenue in response to a consultation document issued by the Department of Trade and Industry in September 2001

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TREASURY SHARES

INTRODUCTION

- 1 We refer to the consultation document published by the Department of Trade and Industry (DTI) in September 2001 and welcome the opportunity to comment on the tax aspects.
- 2 Our comments below are in relation to the tax aspects of the proposal, as set out in section 6 and Annex D. The Institute of Chartered Accountants in England and Wales (ICAEW) has responded directly to the DTI on the company law aspects of the consultation. The responses to the questions set out in Annex D below have also been included in the main ICAEW response.

GENERAL COMMENTS

- 3 We welcome the tax proposals set out in the document. They appear very sensible.
- 4 We regret that the consultation document, which contains important information about proposed changes to the tax rules for share buy-backs, was not available on the Inland Revenue website. Further, there was no cross-reference to it in the Inland Revenue's consultation register. We think that any consultation document which involves tax issues should as a minimum be included in the Inland Revenue's consultation register, linked where necessary to the site which actually contains the document.

RESPONSES TO QUESTIONS SET OUT IN ANNEX D

Paragraph 9 - Treatment of a purchase of shares into treasury

Comments are invited:

i) on whether the current tax treatment of share repurchases should be extended to purchases without cancellation;

- 5 We agree with the proposal to extend the current tax treatment. Given that the commercial impact between:
 - buying shares into treasury and later reselling them; and
 - repurchasing for cancellation and later making a fresh issue of shares

is for all practical purposes identical, we cannot see what other solution could be proposed.

ii) on any practical issues which need to be considered.

- 6 We have no further comments on this question.

Paragraph 11 - Shares held in treasury

Views are invited on the proposal that treasury shares should be excluded from issued share capital for tax purposes, and should also be disregarded when applying tests based on a percentage of issued share capital.

- 7 It is sensible to disregard shares held in treasury when calculating ownership percentages, if only because you will otherwise attribute less than 100% in total to the actual owners. In this respect, the wording of paragraph 6.4 (ii) in the document is not entirely clear. It states:

*... shares held in treasury would be treated **as though** they had been cancelled. Accordingly, they would be excluded from the company's issued share capital for tax purposes and would be disregarded when applying tests based on a percentage of issued share capital ...*

- 8 We would welcome clarification that this means that the shares will be *excluded* from the company's issued share capital when applying tests based on a percentage of issued share capital.

Paragraph 15 - Shares sold from treasury

Views are invited on the proposed treatment of shares sold from treasury.

- 9 We agree with the proposal that shares sold by a company from treasury should be regarded as an issue of shares for the purposes of, for example, capital gains rollover relief on a takeover (section 135, TCGA 1992) and any other reliefs which rely on shares being issued.
- 10 We would welcome clarification as to why the Revenue is said to be reviewing the effect on tax reliefs which depend on an issue of shares. We would also welcome clarification as to the scope of this review; paragraph 6.4 says 'for example in the context of Venture Capital Trusts', while Annex D refers to Venture Capital Trusts (VCTs) exclusively.
- 11 Given the equivalence between 'cancel and reissue' and 'buy into treasury and resell', there appears to be no reason why the proposed company law change should open up areas for tax avoidance. The Enterprise Investment Scheme (EIS) and the Corporate Venturing Scheme already contain extensive rules to prevent relief being given for 'recirculating' what is in reality an existing investment and we do not think that further rules are necessary.
- 12 The highly complicated EIS rules are difficult enough to apply in practice, but the number of investors who need to worry about them is usually very small. The same sort of provisions would be quite inappropriate for the much more widely held VCTs. There is already an anti-avoidance provision (at paragraph 1(9) of Schedule 15B, ICTA 1988) which denies income tax relief for a VCT investment where the

investment was made as part of tax avoidance scheme. We would have thought that this provision was sufficient to counter any abuse.

Paragraph 17 - Stamp duty

Views are invited on the proposed Stamp Duty treatment of repurchases of shares without cancellation and sales from treasury.

- 13 As paragraph 4.3 says, at present when a company purchases its own shares no instrument of transfer is required. Therefore section 66, Finance Act 1986 charges with stamp duty the return (Form 169) delivered to the registrar of companies under section 169, Companies Act 1985. Stamp duty reserve tax (SDRT) is inapplicable because any agreement, oral or written, between shareholder and company for the shares to be repurchased is not an agreement to 'transfer' chargeable securities, within section 87(1), Finance Act 1986.
- 14 A purchase without cancellation is likely to be preceded by an agreement that is arguably liable to SDRT and to involve a proper instrument of transfer, because of section 183(1) of the 1985 Act. Will the stamp duty be collected by a charge on Form 169 or on the transfer? If the former, it will be necessary for Form 169 to cancel the SDRT charge under section 92(1), Finance Act 1986. In order to avoid double taxation, the transfer itself would then need to be exempted. This seems preferable, from a consistency point of view and because it may be unclear at the time of purchase whether the shares will be cancelled or not (see Appendix D paragraph 7).
- 15 When treasury shares are sold, there will doubtless be an agreement liable to SDRT and also a transfer, which presumably will be exempted from stamp duty (as there is no charge on a new issue), either specifically or by means of a new category in the Schedule to the Stamp Duty (Exempt Instruments) Regulations 1987 (SI 1987/516), and which will cancel the SDRT charge.
- 16 If you have any questions, please let us know. We will be happy to discuss any aspects with you further and we would welcome copy of any feedback on this consultation.

FJH
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