

TAXREP 45/05

VENTURE CAPITAL TRUSTS

TAX LAW REWRITE: BILL 4

Memorandum submitted in September 2005 by the Tax Faculty of the Institute of Chartered Accountants in England and Wales in response to an invitation to comment issued in July 2005 by HMRC Tax Law Rewrite Team

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INTRODUCTION

1. We welcome the opportunity to comment on Paper CC(05)21 published on 5 July 2005 by HMRC Tax Law Rewrite Team at <http://www.hmrc.gov.uk/rewrite/exposure/menu.htm>.
2. Details about the Institute of Chartered Accountants in England and Wales and the Tax Faculty are in the Annex.

GENERAL COMMENTS

3. The combining of sections 332A and 842AA of and Schedules 15B and 28B to ICTA 1988 with s 73 FA 1995 and Schedule 33 to FA 2002 in a single rewritten Venture Capital Trusts Part makes access to the VCT legislation much easier for the user. The structure of the Part also makes an understanding of it easier.
4. It is still necessary to refer to the various Regulations, and there will be a need to address the ongoing effectiveness of referring to these from the new Part section numbers.
5. The rewrite is primarily a restructuring of the legislation. As is to be expected with relatively recent source material, extensive redrafting of the text has been found unnecessary. This appears to reflect the improving adoption by the parliamentary draftsmen of the TLR drafting approach, particularly in the rewrite of Schedule 33 to FA 2002 where few changes were made.
6. We note that the draft clauses do not deal with transitional or consequential matters.
7. We also note the provisions relating to VCTs which are not rewritten in the draft clauses, listed in Explanatory Notes paragraph 7, as relating to taxes other than income tax, in the context of Bill 4 as an income tax Bill only.

ANSWERS TO QUESTIONS

8. **Q1** We agree that clause 5(2) should state explicitly that a claim for VCT relief does not have to be by reference to all of the shares in respect of which eligibility exists, in accordance with practice and in particular the explanation in Explanatory Notes paragraph 21.
9. **Q2** We have no objection to the use of the word 'obtained' rather than 'given', consistent with the same expression used in other venture capital schemes in respect of similar material.

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10. **Q3** We agree to the repealing of s 73(3) and (4) FA 1995, as no longer necessary.
11. **Q4** We are content with the drafting of the definition of 'eligible shares' in clause 16(1) (Interpretation of Chapter). The intention of s 73(1)(b) FA 1998 was clearly to omit the word 'preferential' in paragraph 6(1) of Schedule 15B to ICTA.
12. **Q5** Having regard to the detailed analysis in Change {jc 499} in Annex 1, we agree the proposal that different definitions of 'holding' and an 'addition' to a holding are applicable to the 15% holding limit condition in clause 20 and to the rest of the Chapter dealing with VCT approvals.
13. In Annex 1, in the first sentence on page 28, the reference to clause '19(1)' should be to '20(1)' and, in the eighteenth line, the reference to section '842AA(11)(3)(c)' should be to '842AA(11)(c)'.
14. **Q6** It does appear more appropriate to refer in clause 24 to 'tax enactments' rather than perpetuate the paragraph 12(1)(b) Schedule 23 FA 2002 reference to 'enactments'. It will, however, be clear from the regulations themselves which enactment is referred to and, if the use of the term 'tax enactments' would itself require a definition, we have no objection to the rewritten clause 24(1)(b) retaining a reference to 'enactments'.
15. **Q7** We agree the proposal to refer to an officer of Revenue and Customs in relation to the provision of information.
16. **Q8** Agreed – please see our response to Q5.
17. **Q9** We are content with the drafting of clause 29(3) (The maximum qualifying investment requirement), as referred to in Change {jc 497} and in line with current practice. It might be helpful to the reader to point out more clearly in the example in Change {jc 497} that the £1m limit applies to each relevant period and is not an absolute maximum for each qualifying investment. In Explanatory Notes paragraph 112, it might also be helpful to describe 'members' in the third line as 'corporate members' and to describe 'parties' in the fourth line as 'corporate parties'.
18. **Q10** We agree the proposal that clause 32(2) and (6) should provide for the carrying on of a qualifying trade by a company that is not yet a qualifying subsidiary.
19. **Q11** We agree the proposal that clause 32(5)(d) should extend the cases in which research and development can be treated as a qualifying trade.
20. **Q12** We have no objection to the clause 32(9) definition of 'non-qualifying activities', changing the way the exclusion relating to the leasing of ships works by widening the class of ship leasing that is 'permitted leasing'.
21. **Q13** We agree the proposal that clause 33(10) should provide for the carrying on of a qualifying trade by a company that is not yet a qualifying subsidiary.

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22. **Q14** We support the rewriting of paragraph 6(2AB) Schedule 28B ICTA, in clause 35(1), to provide an explicit link with paragraph 6(1) (rewritten in clause 34). Having regard to the analysis in Change {jc 496} we agree that the better view is that paragraph 6(3) is limited to cases where the trade in question is the one that allowed the requirement of paragraph 6(1) to be met.
23. **Q15** We agree the proposal that clause 41(2)(b) should extend the cases in which research and development can be treated as a qualifying trade.
24. **Q16** We agree that it is sensible to align the VCT provisions with those for EIS and CVS in explicitly providing, in clause 41(3), that preparing to carry out research and development does not count as preparing to carry on a qualifying trade.
25. **Q17** We agree that clause 45(5)(b) should refer to ‘the trader’ rather than to ‘the company’ as in paragraph 4(3)(c)(ii) Schedule 28B ICTA.
26. **Q18** We are content with the use in clause 51 of the term ‘business’, as defined by sub-clause 51(5)(b).

SPECIFIC COMMENTS ON DRAFT LEGISLATION

- cl 8 No entitlement to relief which would have been lost if it had already been obtained**
27. Clause 8 correctly rewrites paragraph 8 Schedule 15B ICTA on the basis that had the relief been claimed earlier and it would have been reduced because of circumstances subsequently arising, then there is no entitlement at all to VCT relief. If reduced relief would otherwise have been available, is there a case for now putting forward a PRC to this effect?
- cl 32 The lending requirement**
28. Would it be clearer to simply refer to a disregard of activities for ‘incidental purposes’ which (as clause 32(9) definition of ‘mainly trading subsidiary’) are the only permissible activities of a mainly trading subsidiary apart from activities for the purpose of carrying on one or more qualifying trades?
- cl 34 The use of the money raised requirement**
29. (8)(b) Can the drafting of clause 34(8)(b) be made any clearer?
- cl 43 Meaning of ‘qualifying subsidiary’**
30. Paragraph 10(1) Schedule 28B ICTA requires all subsidiaries of a relevant company with the sub-paragraph 10(3) conditions before any subsidiary can qualify as a ‘qualifying subsidiary’. This requirement does not appear to be rewritten into clause 43.
31. Would it be prudent to include, in the third line of clause 43(5), the words ‘of it’ after ‘subsidiary’ where it first appears?

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cl 52 Power to amend Chapter

32. The Treasury is given power to modify 'sections 32 to 41'. The source legislation, in paragraph 12(a) Schedule 28B ICTA empowers the Treasury to modify paragraphs 3-5. Is it therefore correct to include a power to modify sections 34 (based on paragraph 6), 35 (based on paragraph 6), 37 (based on paragraph 9), 38 (based on paragraph 8) and 40 (based on paragraph 10ZA) without a PRC?

Chapter 5 Powers: winding up and mergers of VCTs

33. With reference to the third bullet point in Explanatory Notes paragraph 7, where will paragraph 4 Schedule 33 FA 2002 (Power to make provision about distributions by VCT-in-liquidation) be rewritten?

cl 56 Power to facilitate disposal to VCT by VCT-in-liquidation

34. Paragraph 5(2)(c) Schedule 33 FA2002 has not been rewritten. We assume that it is intended to include this is due course in the rewrite of capital gains tax.

cl 61 Provision that may be made by regulations under section 60

35. Paragraph 9(1)(c) Schedule 33 FA 2002 has not been rewritten. We assume that it is intended to include this is due course in the rewrite of capital gains tax.

cl 64 Interpretation of Chapter

36. Why is the paragraph 17 Schedule 33 FA 2002 definition of 'company', which applies for the purposes of FA 2002 Schedule 33 (rewritten in clauses 54-64), excluded from clause 64?

DETAILED COMMENTS ON DRAFTING

cl 6 Form and amount of relief

37. (1)(a) The second 'is' should be deleted.

cl 22 Conditions relating to qualifying holdings and eligible shares: supplementary

38. Explanatory Notes paragraph 78 refers to a signpost (to the definition of ordinary share capital) in clause 73 which does not appear in clause 22 as drafted.

cl 28 Introduction

39. In clause 28(3)(g) omit the first 'qualifying'.
40. In Explanatory Notes paragraph 105, the word 'and' at the beginning of the third line needs to be moved to come before 'clause 35' at the end of the second line.

cl 35 The relevant qualifying activity to be carried on by the relevant company requirement

41. In Annex 1, in Change {jc 496}, in the third paragraph from the end, should the two references to 'paragraph 6(3)' be to 'paragraph 6(2AB)'?

cl 36 The unquoted status requirement

42. In Explanatory Notes paragraph 144, in the second line, the reference to 'paragraph 5(6)' should be to 'paragraph 2(6)'.

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cl 37 The control and independence requirement

43. In Explanatory Notes paragraph 146, in the first line, the reference to ‘paragraph 8’ should be to ‘paragraph 9’.

cl 38 The gross assets requirement

44. In the first line, insert ‘a’ before ‘relevant’.

cl 41 Meaning of ‘qualifying trade’

45. In Annex 1 Change {jc 498}, in the fourth line on page 44, ‘VCT’ should read ‘CVS’.

cl 42 Meaning of ‘qualifying 90% subsidiary’

46. (4)(b) Should the word ‘including’ be retained before ‘references’ in the second line of clause 42(4)(b), as in paragraph 5(6)(b) Schedule 28B ICTA?

cl 44 Meaning of ‘excluded activities’

47. In Explanatory Notes paragraph 164 the reference to ‘paragraph 4(1)’ should be to ‘paragraph 4(2)’.

48. Section 46 should be listed before section 47.

cl 45 Excluded activities: wholesale and retail distribution

49. The unattributed origin of clause 45(2) is ‘Drafting’.

cl 47 Excluded activities: leasing of ships

50. In the first line, ‘seciton’ should be ‘section’.

cl 52 Power to amend Chapter

51. In clause 52(b), the reference to ‘section 29(3)’ should be to ‘section 29(2)’.

cl 53 Interpretation of Chapter

52. (7)(c)(i) In clause 53(7)(c)(i), in the first line, the second ‘a’ should read ‘at’.

cl 62 Meaning of ‘merger’ and ‘successor company’

53. With reference to Explanatory Notes paragraph 194, clause 62 is based on the whole of paragraph 10 of Schedule 33 to FA 2002 rather than on paragraph 10(1) only.

cl 65 Restructuring to which section 66 applies

54. In Explanatory Notes paragraph 201, the three references to ‘EIS’ relief should be to ‘VCT’ relief.

cl 70 ‘Winding up’ of the relevant company

55. In Explanatory Notes paragraph 209, in the second line, insert ‘were’ before ‘not’.

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WHO WE ARE

The Institute of Chartered Accountants in England and Wales ('ICAEW') is the largest accountancy body in Europe, with more than 128,000 members. Three thousand new members qualify each year. The prestigious qualifications offered by the Institute are recognised around the world and allow members to call themselves Chartered Accountants and to use the designatory letters ACA or FCA.

The Institute operates under a Royal Charter, working in the public interest. It is regulated by the Department of Trade and Industry through the Accountancy Foundation. Its primary objectives are to educate and train Chartered Accountants, to maintain high standards for professional conduct among members, to provide services to its members and students, and to advance the theory and practice of accountancy, including taxation.

The Tax Faculty is the focus for tax within the Institute. It is responsible for tax representations on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter 'TAXline' to more than 11,000 members of the ICAEW who pay an additional subscription.