Finance Bill 2024-25
Clause 31 and Sch 6 Employee Ownership Trusts

BRIEFING FOR MPS ON THE FINANCE BILL BY ICAEW TAX FACULTY

WHO WE ARE

Please see Appendix 1.

EXECUTIVE SUMMARY

1. This briefing relates to the measures included in the Finance Bill to change the tax rules relating to employee ownership trusts.
2. A new s401ZA, Income Tax Trading and Other Income Act 2005 (ITTOIA 2005) allows a claim to be made to deduct trustees' acquisition costs from any taxable distribution made on or after 30 October 2024 where that distribution is received from the target company to facilitate the purchase by the trust of the company's shares under an employee ownership trust arrangement. However, we believe that there are a much wider sets of costs that might be incurred by the trust, both in acquiring the shares and in managing its shareholding. We believe that the expenses covered under the claim need to be defined more widely to prevent unintended tax liabilities arising in the trust.

THE MEASURE

3. Schedule 6 to the Finance Bill includes various measures designed to change the rules relating to employee ownership trusts. This includes para 9 which introduces new s401ZA, ITTOIA 2005. This is designed to prevent an income tax liability arising in the trust that purchases the shares of a company in such arrangements. This liability can arise because payments are often received by the trust from the company to help it to purchase the company's shares and pay for associated expenses.
4. Technically, such payments are 'distributions' within the meaning of s1000, CTA 2010. Section 383, ITTOIA 2005 requires such distributions to be taxed as income. However, HMRC has historically granted clearances to confirm that it would not seek to treat such distributions as taxable in the hands of the trustees. HMRC has confirmed that it will no longer provide these clearances and will require taxpayers to rely on s401ZA instead for distributions made on or after 30 October 2024.
5. Subsection (2) of that section allows the trustees to make a claim that its acquisition costs may be deducted from the taxable distribution.
6. The trustees' acquisition costs are defined at subsection (4) as:
   "(a) the consideration for the disposal,
   (b) where some or all of the consideration for the disposal is deferred, so much of any interest payable in relation to the deferral as reflects a rate of interest not exceeding a reasonable commercial rate, and

(c) any liability to stamp duty or stamp duty reserve tax on the acquisition of the ordinary share capital."

OUR CONCERN AND OUR RECOMMENDATIONS

7. We are concerned that the relief does not extend to other associated costs of the trust, both in relation to the acquisition of the shares in the company and the ongoing management of its shareholding. These include, but are not limited to the following:

    a) Professional fees incurred on acquiring the shares, particularly given the new requirements under the proposed s263H (4) (ca) TCGA 1992 for the trustees in relation to the sales price and interest rates.
    b) Financing fees, particularly if there is third-party debt involved in the transaction.
    c) Fees paid to professional trustees to ensure that the trust is managed independently from the former owners and that there is sufficient expertise among the trustees to manage the trust effectively.

8. We consider that new s401ZA, ITTOIA 2005 should be extended to include the expenses identified above, along with other legitimate and reasonable expenses of the trust.
9. As the trust is intended to be managed for the benefit of the employees of the company, this change would ensure that intention is better met by avoiding the trust incurring tax liabilities and funding the costs identified above out of 'after tax' income.

SUGGESTED AMENDMENT

10. We believe that the definition of trustees' acquisition costs at new s401ZA(4), ITTOIA 2005 should be extended to also include any other expenses legitimately incurred or to be incurred by the trustees in acquiring the shares and the performance of their duties to manage the trust and the assets of the trust for the overall benefit of the beneficiaries.

FURTHER INFORMATION

As part of ICAEW's Royal Charter, we have a duty to inform policy in the public interest.

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APPENDIX 1

ICAEW TAX FACULTY – WHO WE ARE

Internationally recognised as a source of expertise, ICAEW's Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 169,000 chartered accountant members in over 146 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.