

# Newsletter

## HMRC PUTS THE SQUEEZE ON MVL's

### LAST WEEK HMRC ANNOUNCED PROPOSED CHANGES TO TAX RULES ON DISTRIBUTIONS TO SHAREHOLDERS IN A WINDING –UP

With the changes in taxation of dividends due to commence on 6 April 2016, HMRC have stepped in to block a perceived loophole in the current legislation. They are worried that the practice has arisen, where the director/shareholder of small companies allow cash to accumulate in the Company bank account and then extract it by way of a distribution in a solvent Members Voluntary Liquidation (MVL). The shareholder takes advantage of Entrepreneurs Relief, thereby paying only 10% tax on the capital distribution.

HMRC have published a Policy Paper and draft legislation

<https://www.gov.uk/government/publications/corporation-tax-income-tax-and-capital-gains-tax-company-distributions/corporation-tax-income-tax-and-capital-gains-tax-company-distributions>

These rules make it clear that what they are trying to prevent is the shareholders obtaining a tax advantage by a mechanism where a main purpose, or one of the main purposes is to obtain a tax advantage. They also set out a new Targeted Anti-Avoidance Rule (TAAR) aimed specifically at MVL's.

Under the new TAAR a distribution from a winding up will be treated as an income distribution where three conditions are met:-

- The individual (S) who is a shareholder in a close company (C) receives a distribution in respect of shares in a winding-up

*(presumably either in the form of cash or a distribution in specie)*

- Within a period of two years from the date of the distribution S continues to be involved in a similar trade or activity (*either directly or through an associate*)
- The circumstances surrounding the winding-up have the main purpose, or one of the main purposes, of obtaining a tax advantage.

## DOES THIS PUT AN END TO MVL's?

Well no. It does however mean that more thought needs to be put into the process. What HMRC are worried about is so called Phoenixing MVL's, whereby a director/shareholder uses the MVL process to close down the company they trade through every few years, starting a new one immediately afterwards. In the process, no doubt taking minimum salary and dividend and utilizing their Entrepreneurs Relief to minimize the tax they pay.

There are two areas to concentrate on:-

- The two year Rule and
- The main purpose, or one of the main purposes of the winding up.

## THE TWO YEAR RULE

It would appear that if a director/shareholder wishes to take advantage of the MVL process, the easiest way to ensure that the TAAR do not apply will be to obtain PAYE employment, or in the contracting sector, work through an Umbrella Company, for two years following the final distribution. This way Condition B is not breached.

It is not clear at this stage whether or not there will be any transitional provisions. This could be an issue since many liquidators pay 98% of the sums available for distribution almost immediately after the commencement of the liquidation, with only a small contingency being retained. Once HMRC have confirmed the tax position, the balance of funds are distributed. Currently HMRC are taking up to 6 months to confirm the tax position.

In our view it would be more appropriate for these new rules to apply only to those individuals whose company commenced winding up on or after 6 April 2016. Otherwise there is a danger that some individuals could be caught out by a regulation that didn't exist at the time they embarked on the liquidation process.

## MAIN PURPOSE OR ONE OF THE MAIN PURPOSES

In our experience tax is one of the reasons, but not always the main one, behind a MVL. The vast majority of the shareholder/directors we have dealt with have wanted to close their company down for a legitimate commercial reason. The most common reasons are retirement, obtaining PAYE employment and therefore no longer needing the company and to cap any potential liability for claims.

In future it may be prudent for advisers to document this thought process and provide written advice to the Company, as this could become relevant in any Tax Enquiry. It may also have some bearing on the way in which accountants market this service in future. If the main purpose is tax avoidance then the shareholder/director will need to be warned that they must not breach Condition B, the Two Year Rule.

## WHAT NEXT?

We anticipate that anyone contemplating doing a MVL will want to get it done and have received the distribution by 5 April 2016.

It needs to be remembered that to fall foul of the TAAR all three conditions must be met. From a brief discussion with HMRC it is clear that the legislation is designed to deter the serial MVL user, whose main purpose is to obtain a tax advantage. What is apparent is that they will look closely at Conditions B and C. Thus where the main purpose for the MVL is retirement, or because a contractor is now becoming a PAYE employee that should provide the necessary justification, even if the individual subsequently set up a new company within the two year rule set out by Condition B. They would have to be able to demonstrate what their main purpose(s) was/were for liquidating the company. However there seems, at this early stage at least, to be a recognition that events often take over and people lose their jobs and may be forced back into contracting through a personal service company.

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If this may affect any of your clients and you need to discuss any points raised in this newsletter, telephone Mike Simister, Neil Henry or Lisa McAllister on 0161 929 1905 or email: [Mike@lineshenry.co.uk](mailto:Mike@lineshenry.co.uk)

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