14 September 2026

Modernising the taxation of distributions and repayments of capital from companies

Response from ICAS

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1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants. We represent over 24,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice. Approximately 12,000 of our members are based in Scotland and 10,000 in the rest of the UK.

2. The following submission has been prepared by the ICAS Tax Board. The Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community; it does this with the active input and support of over 60 committee members.

3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and regulatory system design, and to point out operational practicalities.

General comments

4. We welcome the opportunity to respond to the HMRC consultation Modernising the taxation of distributions and repayments of capital from companies - GOV.UK

Specific Questions

Question 1: How do any of the proposals outlined in this document impact Corporation Tax payers?

5. We have no comments on this question.

Question 2: What general comments do you have on the proposal to modernise the rules determining the size of a distribution on a reduction of share capital or share buyback?

6. We have received member feedback that the Example (John) is flawed, as share premium would not be created on such a transaction. The 'premium' would technically be accounted for with a credit to a merger reserve, which on its own cannot be reduced. The 2015 HMRC consultation Company distributions - GOV.UK included a similar example (Gavin Industries Ltd) addressing the same concern. In 2016 the transactions in securities ('TiS') rules were strengthened as a result of the 2015-16 consultation process with the insertion of CTA 2010 paragraphs 686(e) and (f) to include repayments of share capital or share premium, and distributions in respect of securities on a winding up within the definition of 'transactions in securities'.

7. The outcomes in both examples noted above are distortive but we suggest that more targeted anti-avoidance rules could be used to counter the specific tax advantages that HMRC may be concerned about (e.g. the tax capital uplift in certain circumstances) rather than the general changes proposed. We believe that the current TiS rules already act as an effective and appropriate deterrent to this tax planning.

8. Any taxpayer undertaking this planning with the intention of later repaying share capital would be required to fully disclose this intention when applying for a clearance under TCGA 1992 s.138, and HMRC would be able to refuse a clearance or counteract under TCGA 1992 s.137 in appropriate cases.

9. We have concerns that the proposal to freeze the "tax capital" on shares will have adverse consequences on commercial reconstructions. Feedback we have received suggests that there is uncertainty around the extent to which the planning of inserting a holding company in advance of

a repayment of capital referred to in the consultation is being used or recommended to clients by tax practitioners.

10. In the absence of any data which HMRC may hold as to the extent of the perceived problem, what is proposed seems to be a policy “sledgehammer to crack an imaginary nut” which will have the more serious consequence of rendering capital reduction demergers redundant as discussed later in this submission. We suggest that a more targeted anti-avoidance rule could be introduced to address any real concern HMRC has around this specific tax planning activity instead of the proposed approach.

Question 3: Please describe how this proposal might impact legitimate corporate demergers and share restructuring.

11. Capital reduction demergers have become a well-known and important tool for private companies since 2008 when capital reductions using the solvency statement procedure became effective for these companies. We understand that these forms of demerger have almost entirely replaced the more costly Insolvency Act 1986 s.110 liquidation demerger route, which can achieve the same results to demerge non-trading businesses and to effect demergers prior to a commercial sale of a business.

Question 4: Can you anticipate any other unintended or unwelcome consequences of this proposal, such as on third party sales?

12. Taxpayers gain flexibility to deploy capital reduction demergers in more situations than either liquidation or statutory demergers alternatives. The proposals in the consultation could ‘wind the clock back on corporate reconstructions almost 20 years’, significantly reducing this flexibility for private companies and increasing costs for taxpayers, who will inevitably revert back to liquidation demergers.

13. A wealth of practical experience has been built up by professionals using these structures. The concern around repayments of capital contained in the consultation, absent any data on how widespread HMRC’s specific concern may be, might suggest that the proposal to remove capital reduction demergers is a disproportionate response that risks making that wealth of experience redundant.

14. We have concerns that this proposal risks countering legitimate business planning by people running their own business, having taken personal and financial risk and made other sacrifices to do so. This risks disincentivising investment and entrepreneurial activity and a detrimental impact on economic growth. On the contrary, we believe that the tax system should encourage such activity and economic growth.

15. We agree that there are potential challenges, as outlined in the consultation on third party share sales and share for share exchanges within groups or the Substantial Shareholding Exemption (SSE) applies which should be carefully considered as a potentially detrimental consequence of these proposals.

Question 5: In what scenarios would you currently undertake or recommend a non-statutory demerger?

16. Member feedback we have received indicates that non-statutory demergers are used in wide ranging scenarios and are the most common form of corporate reconstruction for private companies.

    These include:
    - Separating trading from investment activities.
    - Separating one business in a group to facilitate a ‘clean’ sale of the majority of the group’s activities.
    - Partitioning private groups between different shareholders.

Question 6: Do you think that the statutory demerger rules ought to apply to a broader scope of transactions?

17. Yes, we believe that the statutory demerger rules should be amended to apply to a wider range of transactions, particularly if the government decides to remove the capital reduction route. We believe that the conditions for the statutory demerger route are too restrictive and act as a barrier to widespread use of the statutory route.

18. We would support the removal of all restrictions, ie going further than the proposals in the consultation, especially in light of the strengthening of TCGA 1992 s.137, which could potentially encourage more taxpayers into the statutory route. As noted below, we have concerns that some of the proposed changes amount instead to further restrictions on the statutory route.

Question 7: What comments and suggestions do you have regarding the amendments suggested above to the statutory demerger legislation?

19. The distinction between trading and investment activities in the statutory demerger rules is outdated. We therefore welcome the proposed update to condition B to include investment businesses as well as trading businesses.

20. We have concerns regarding the proposed changes to condition D. The proposals concerning onward sales and changes in control risk creating unintended consequences and could significantly hamper genuine commercial transactions that can be carried out under current legislation and practice.

21. Condition D currently requires that no demerger can be used to facilitate an onward sale – the consultation proposes that this would be changed so that the restriction would apply to onward sales within 5 years of the demerger. However, there would be an exception to the 5 year restriction for cases where all trading activities are disposed of. This will significantly hamper commercial sales and therefore not help to prevent an over-reliance on non-statutory practices, a goal stated in the consultation. For example, under the current rules it can be possible for an unexpected offer for a business (or part of it), which the taxpayer can demonstrate was not contemplated at the time of the demerger, to be made and accepted within 2 years from that date. The proposed change would largely put the demerger relief out of reach if it falls outside the proposed exclusion for sales of the whole trade within the five-year period.

22. We have received member feedback that the comment "…what is commonly accepted as normal succession planning in family businesses…" does not reflect their experience in practice.

Question 8: Are there any other specific parts of the legislation which you think the government should re-examine?

23. We understand that the chargeable payments rules are not well understood and cause significant concern and uncertainty for clients following the implementation of a statutory demerger. The reasons for retaining these rules remain unclear and we believe they would continue to create commercial uncertainty.

Question 9: In what way do you think the demerger rules ought to be liberalised in order to account for the removal of capital demergers?

24. We believe that all restrictions should be removed and a rule based on TCGA 1992 s.139(4A) to align with practice in that area should be introduced.

Question 10: Do you anticipate any unintended consequences as a result of the proposals set out in this chapter?

25. See our response to Question 7.

Question 11: Do you have any general comments on aligning the charge to Income Tax on distributions from non-UK resident companies with the rules that already apply to distributions from UK-resident companies?

26. We agree that in principle it makes sense to explore aligning the tax treatment. However, as the consultation notes there could be issues for taxpayers, for example where UK and overseas corporate law differ. If the government decides to proceed with these proposals, HMRC will need to provide comprehensive and effective guidance to accompany the new rules. This guidance should include coverage of interactions with other regimes, for example the Foreign Income and Gains regime.

Question 12: Can you foresee this proposal having any impact on obtaining relief for double taxation where the distribution is subject to tax in another state?

27. We have no comments on this question.

Question 13: Do you anticipate this proposal deterring any commercial corporate actions? If so, please provide details and suggestions of how this impact could be addressed

28. We have no comments on this question.

Question 14: Do you have any comments on the proposal to extend the charge to stock dividends? In particular, are there difficulties with the classification of shares in non-UK jurisdictions?

29. We have no comments on this question.

Question 15: Do you have any comments on extending the charge to redeemable bonus shares and securities?

30. We have no comments on this question.

Question 16: Do you have any comments on to what extent the charge to Income Tax on distributions should apply to payments on special securities and non-commercial securities?

31. We have no comments on this question.

Question 17: Do you have examples of where instruments that would be treated as special securities and non-commercial securities are used in existing structures where the return would be paid to UK residents within the charge to Income Tax?

32. We have no comments on this question.

Question 18: Do you have any comments on the potential tensions between the definitions used in the UK distributions rules and non-UK corporate legislation, especially with regard to the distinction between income and capital? In particular, are there any difficulties around what constitutes a 'repayment of capital'? How could these be addressed?

33. We have no comments on this question.

Question 19: Do you have any insights from other jurisdictions which also use the capital/income divide in their tax legislation?

34. We have no comments on this question.

Question 20: Are you aware of any particular existing difficulties around whether a distribution from a non-UK incorporated company is a 'dividend'? Should the government consider introducing provisions to clarify the treatment where the non-UK company law is unclear?

35. We have no comments on this question

Question 21: When calculating what amount of a distribution is a repayment of capital, would it be effective to permit small shareholders in widely held or quoted companies, who do not have access to the necessary information, to simply use the nominal value of the interest they hold on a share buyback? Are there difficulties with calculating the nominal value of the share in some jurisdictions?

36. We have no comments on this question.

Question 22: Are you aware of instances where dividends or other distributions have been improperly paid? If so, were the distributions repaid to the company and on what timescale? What was the tax treatment generally adopted on the repayment?

37. We have been made aware that in scenarios where a buyback has not been done correctly and the company lawyer indicates that the transaction is voidable, the amount of the 'distribution' is instead treated as a loan, which creates a CTA 2010 s.455 charge with the loan being repaid/written off at a later date.

38. We have also been made aware that due diligence in advance of a company sale identifies an erroneous distribution resulting in an overdrawn loan account, this can often be dealt with as part of the sale process.

Question 23:Would priority rules to establish what the primary charge will be on an extraction address the issue? Are there any adverse consequences to this?

39. We have no comments on this question.

Question 24: Do you have any views as to whether legislating for the current discretionary practice of unwinding unintentional gratuitous transfers would provide a solution?

40. We believe that Option 2 is a sensible proposal and that it would be useful to put the discretionary practice referred to on a statutory footing. Clear guidance from HMRC should be available for taxpayers if this option is progressed.

Question 25: What are your views on allowing Income Tax paid on an unlawful distributions to be set off against liabilities incurred on rectifying the issue?

41. We believe that Option 3 (enabling income tax paid on extractions to be set off against liabilities incurred on rectifying the payment at a later date) has considerable merit.

42. As the consultation notes, by the time the second charge to Income Tax arises, it may be too late for the shareholder to be able to claim relief for the tax paid on the original distribution, giving rise to double taxation, which is undesirable.

Question 26: What alternative solutions might be implemented to address the issues raised in this chapter?

43. We have no comments on this question.

Question 27: Given that the tax would need to be paid by individuals rather than by the companies making the loans, would this result in particular administrative difficulties? If so, please provide examples.

44. We have concerns about imposing the liability on the individual, who may well have borrowed from the company to meet their financial needs, so may not have sufficient funds to pay the tax. This could lead to additional borrowing to pay the tax which seems to result in an unsatisfactory 'circular' position.

45. We are concerned that tax charges may arise in respect of loans from hybrid entities where the other jurisdiction does not recognise a taxable transaction. If the lending company is tax resident in a jurisdiction which imposes a charge on the company in the nature of that imposed by the UK loans to participators regime, there is potential for double taxation with no treaty mechanism to resolve the position.

46. It is unclear how any tax charge in respect of loans made by non-UK resident companies would be proposed to interact with the Foreign Income and Gains regime. This should be carefully considered, were these proposals to be taken forward.

Question 28: What general comments do you have on the proposal to introduce a temporary tax on loans received from non-UK resident closely controlled companies?

47. We support this proposal in principle in order to remove a potentially distorting and inequitable situation. We believe that careful consideration of the details will be required when designing the provisions. See also our response to Question 29.

Question 29: Do you have any specific comments on the four options outlined above? Do you have any suggestions as to what time periods would be appropriate?

48. We believe that option 3 (potentially with option 4) is preferable as it removes any initial charge to income tax, as noted above.

49. However, careful consideration should be given to how any proposed rules will work, for example, in the context of internationally-mobile individuals whose residence status changes from UK resident to non-UK resident while the amount is outstanding.

Question 30: The close company definition is extremely broad. Can you see this proposal affecting loans made on arm's length terms to participators with very minor interests, and if so, can you provide examples?

50. We have no comments on this question.

Question 31: What impacts would the proposal have on arm's length commercial lending?

51. We have no comments on this question.

Question 32: Would limiting this charge to participators and their associates of participators with material interests in the overseas companies help to target this at loans which represent extractions of profit?

52. We have no comments on this question.

Question 33: if we expand the exclusion for loans or advances made in the ordinary course of business, what changes would be necessary to avoid curtailing normal commercial activity?

53. We have no comments on this question.

Question 34: What general comments do you have on the proposals set out in this chapter?

54. We understand that the subjectivity of the trade benefit test causes issues in applying the rules to commercial scenarios, in particular, the substantial reduction test seems redundant when HMRC expect the departing shareholder to fully dispose of their shareholding in almost all scenarios, absent a sentimental retained shareholding. However, practitioners have significant practical experience in applying the rules and the proposed changes could have unintended consequences and lead to more 'Newco' buyouts instead of share buybacks.

55. We believe that the proposed imposition of a minimum 5% shareholding and employment by the company for two years prior to the shareholder departure is a material narrowing of the conditions

to obtain capital treatment. This change would remove the facilitation of exits of non-employee shareholders or non-individual shareholders such as trusts or executries/estates.

56. We are unsure as to why this two-year period is proposed, and we are also unsure about the reasoning behind the requirement that phased exits must be completed within a two-year period. The latter appears disproportionately restrictive in what are in many cases, contentious circumstances, with the exiting shareholder not always in control of how the exit is managed. In the case of phased exits, we are unclear how any adverse cash flow implications resulting from an income tax liability arising on an exit under the proposed changes could be mitigated.

57. It is not clear to us why a shareholder with a 4% shareholding should be further disadvantaged over a 5% shareholder who could obtain capital treatment under the proposed changes. A 4% shareholder is already denied Business Asset Disposal Relief (BADR) on a share buyback (unless they have acquired their small shareholding via an EMI scheme), so removing the possibility of capital treatment whatsoever seems inequitable.

58. We believe that the costs of requiring a share valuation will be disproportionate for small businesses and that clear guidance should be provided regarding the reasonable steps the company must take to ensure that consideration does not exceed market value. We also note that there is already a requirement for a company to ensure that this rule is met for employment-related securities.

59. We note that the consultation states that there is no intention to change Condition B in CTA 2010 s.1033. However, we have received feedback from members suggesting that this is something the government should consider in light of the recent changes to inheritance tax (IHT) reliefs (BPR and APR) and the consequent increased likelihood of family trading businesses and farms facing additional IHT exposure. The undue hardship requirement of Condition B could be relaxed to facilitate access to capital treatment where the buyback is necessary to fund increased IHT liabilities resulting from the changes to APR and BPR.

Question 35: What unintended consequences do you anticipate as a result of these changes?

60. We understand that the proposed changes would reduce the scope for exits from employee incentive schemes, such as hurdle or growth shares. This could lead to the reduced implementation of these schemes which can be key for growing companies to retain and incentivise staff.

61. The proposed change to withdraw capital treatment where an exiting shareholder (perhaps as a result of retirement) returns as a director (without any access to share capital or dividends) could impact genuine corporate rescue scenarios and prevent a distressed business from bringing back key people who could help their recovery. For example, a shareholder/director may take parental leave from running the business which may require a former shareholder with experience of the business to return from retirement, or in potentially more difficult scenarios, following the decease of the shareholder/director running the business.

62. The five year period preventing returns in certain circumstances, similar to those noted above, seems unnecessarily restrictive and risks the survival of family businesses facing such circumstances.

Question 36: What general comments do you have on the proposal set out in this chapter?

63. We are unclear as to the specific reasons why HMRC believes the long-standing, though evolved, TiS regime is not fit for purpose. The experience shared with us is that the submission of clearances on behalf of clients works well, the outcome illustrates what planning works or not, and that there has generally been success for HMRC in TiS related disputes in the Courts.

64. The member feedback we have received includes the suggestion that further alignment with self-assessment processes (as previously noted in the 2015 consultation [Company distributions - GOV.UK]) may be one element of the regime that HMRC is looking to change. There is a strong

view that if further alignment with self-assessment is in fact an HMRC objective, practitioners would nonetheless value the retention of the ability to obtain clearance in advance.

65. We also note that the consultation is light on specific detail on the proposed changes beyond introduction of “an updated anti-avoidance regime”. We believe that a more beneficial outcome from this consultation process could be achieved if it was clearer what the specific problem(s) or issue(s) that HMRC have with the current regime are. This would enable stakeholders to provide more specific input as to potential alternatives to resolve the issue(s) or problem(s).

Question 37: What unintended consequences do you anticipate as a result of this proposal?

66. As noted in our response to Question 36, we believe that the current TiS rules work well, largely due to the ability to apply for a statutory clearance under ITA 2007 s.701 in advance of the transaction, and the existence of the current “safe harbours” in the legislation. We consider that any replacement of the current rules without these features would not be a positive development. Taxpayers and their advisers require certainty. We have concerns that the removal of safe harbours and a statutory clearance regime, even with clear and substantial guidance, risks leaving tax advisers exposed to greater risk, particularly in light of the recent enhancement of HMRC powers for non-compliant advisers and mandatory tax adviser registration requirements.

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