

Entrepreneurs' Relief

Entrepreneurs' Relief was introduced in 2008 and whilst there have been changes to the amounts qualifying for relief, the basic scheme has remained unchanged since its introduction. This reflects the changes to the lifetime allowance announced in the Budget on 11 March 2020. It has also had a change of name and is now Business Asset Disposal Relief.

There is a limit on the value of qualifying gains that can benefit from Business Asset Disposal Relief (Entrepreneurs' Relief). An individual has a lifetime allowance of £1million of qualifying gains. The lifetime allowance may be claimed in full on one disposal, or may be claimed in respect of a number of different disposals across a number of tax years until the lifetime limit is reached.

A claim for Business Asset Disposal Relief (Entrepreneurs' Relief) with respect to a particular qualifying disposal is applied to the net aggregate qualifying business gains (NAQBG). The NAQBG is the aggregate of the total relevant chargeable business gains and losses from the specific disposal. This is more relevant when a partnership interest is sold than for a sale of company shares.

The legislation provides that any capital gain that qualifies for Entrepreneur's Relief is chargeable at a flat rate of 10%.

Business Asset Disposal Relief is an all or nothing claim and is automatically the lower of the NAQBG and the lifetime allowance not previously utilised. It is not possible to specify a lower amount. Accordingly, where it is anticipated that future qualifying gains will be made, it may be preferable not to claim Business Asset Disposal Relief if making the claim would result in a portion of the annual exemption being wasted.

Provided the qualifying conditions are met and the lifetime limit has not been exhausted Business Asset Disposal Relief will be available.



Interaction with losses

Where a claim is made with respect to a qualifying business disposal any losses arising from the disposal will reduce the gains and it will be this amount (referred to above as NAQBG) that qualifies for Business Asset Disposal Relief. Losses on other disposals or brought forward losses will be deducted from this amount, although the legislation includes specific provision to allow the loss offset to be allocated in the most beneficial manner. This means that losses should be deducted from gains chargeable at 28% or 20%, before being deducted from gains qualifying for Business Asset Disposal.

Qualifying conditions

For a gain to qualify for Business Asset Disposal Relief, the disposal must meet the qualifying business asset disposal criteria. Certain conditions must be met with respect to the significance of the disposal and the period of time that the taxpayer has held the asset. Disposal of an asset used for business purposes without there also being a disposal of the whole or part of that business will not qualify for relief.

There are three categories of qualifying business disposals:

- A material disposal of a business asset.
- A disposal of trust business assets.
- A disposal associated with a relevant material disposal.

The notes overleaf focus on the first category of qualifying disposal and additional information is available on the other categories if required.

Material disposal of a business asset

There must be both a qualifying holding period and a material disposal. For there to be a qualifying holding period, the business or the company must be owned by the individual throughout the two years ending with the date of the disposal. If the disposal occurs within three years of the company ceasing to be a trading company or a member of a trading group, the holding period qualification must be met throughout the two years ending with the cessation of trading.

The following qualify as material disposals of business assets:

- The disposal of the whole or part of a business (including a partnership interest). Retirement relief case law is relevant in determining what constitutes a part of a business as HMRC consider the same principles apply when considering Entrepreneurs' Relief.
- The disposal is of (or of interests in) one or more assets in use for the purposes of the business, at a time when the business ceased to trade and the disposal occurs within three years of the business ceasing to trade.
- Assets consisting of (or of interests in) shares in or securities of a company where the company is the individual's personal company (see below) and the individual is an officer or employee of the company or one or more companies which are members of the trading group. There is no minimum working time requirement and non-executive directors and the company secretary can therefore qualify, provided they have been properly appointed through the filing of the appropriate Companies House forms.

An individual's personal company is either a trading company or the holding company of a trading group in which the individual:

- owns at least 5% of the company's ordinary share capital
- exercises at least 5% of the company's voting rights
- and meets either the equity test or a test based on entitlement to sale proceeds.

The equity test requires the shareholder to be entitled to at least 5% of the amounts available for distribution to equity holders and at least 5% of the assets available for distribution to equity holders on a winding up. The definition of equity holders includes loan creditors other than normal commercial loans and therefore this test needs to be reviewed at the time of sale to determine if the test is met.

The alternative test is based on an individual's entitlement to at least 5% of the sale proceeds on a sale of the entire ordinary share capital. This is a notional test which can then be applied to a partial disposal of shares.

Provided an individual meets these tests throughout the qualifying period, additional shares and securities can be held for a shorter period with Entrepreneurs' Relief being available on the entire disposal provided the lifetime limit is not exceeded. This can be particularly helpful in relation to spouse shareholdings. An individual who acquires their shares as part of an Enterprise Management Incentives (EMI) scheme, may qualify on holdings of less than 5%. Please seek further advice if this applies to you.

For a sale of shares or securities it is not necessary for the individual to dispose of his or her entire shareholding; provided the qualifying conditions (explained above) are met, Entrepreneurs' Relief will be available (subject to the limit imposed by the lifetime allowance) on a sale of some or all of the shares or securities.

The definition of a trading company is the definition used for the purposes of the gifts of business assets and holdover relief provisions. Generally any commercial activity undertaken with a view to profit should qualify as a trading activity for these purposes, although trades which are heavily based on property should ask for further advice to determine whether they will be treated as a trading company.

There is no requirement that the company must be a UK company but where an overseas vehicle is used it will be important to consider whether it will meet the qualifying conditions. As the individuals must be both 5% minimum shareholders and directors/employees of the business this may affect the control and management tests for the overseas business and the total tax position should be reviewed accordingly before any decisions are taken.

There are further specific rules regarding any reorganisation of the company or business and how Business Asset Disposal Relief interacts with other reliefs which are not considered in this document.

Please note that this factsheet is for general information purposes only. Professional advice should be obtained before action is either taken or refrained from as a result of information contained herein. Date created: 1.9.2020