



Finance Act 1989

1989 CHAPTER 26

PART II

INCOME TAX, CORPORATION TAX AND CAPITAL GAINS TAX

CHAPTER III

CAPITAL GAINS

Value shifting and groups of companies

136 Value shifting: reductions attributable to distributions within a group

(1) After section 26 of the Capital Gains Tax Act 1979 there shall be inserted—

“26A Value shifting: distributions within a group followed by a disposal of shares

- (1) The references in section 26 above to a reduction in the value of an asset, in the case mentioned in subsection (7) of that section, do not include a reduction attributable to the payment of a dividend by the second company at a time when it and the first company are associated, except to the extent (if any) that the dividend is attributable to chargeable profits of the second company and, in such a case, the tax-free benefit shall be ascertained without regard to any part of the dividend that is not attributable to such profits.
- (2) Subsections (3) to (11) below apply for the interpretation of subsection (1) above.
- (3) Chargeable profits shall be ascertained as follows—
 - (a) the distributable profits of any company are chargeable profits of that company to the extent that they are profits arising on a transaction caught by this section, and

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- (b) where any company makes a distribution attributable wholly or partly to chargeable profits (including any profits that are chargeable profits by virtue of this paragraph) to another company, the distributable profits of the other company, so far as they represent that distribution or so much of it as was attributable to chargeable profits, are chargeable profits of the other company,

and for this purpose any loss or other amount to be set against the profits of a company in determining the distributable profits shall be set first against profits other than the profits so arising or, as the case may be, representing so much of the distribution as was attributable to chargeable profits.

- (4) The distributable profits of a company are such profits computed on a commercial basis as, after allowing for any provision properly made for tax, the company is empowered, assuming sufficient funds, to distribute to persons entitled to participate in the profits of the company.
- (5) Profits of a company (“company A”) are profits arising on a transaction caught by this section where each of the following three conditions is satisfied.
- (6) The first condition is that the transaction is—
- (a) a disposal of an asset by company A to another company in circumstances such that company A and the other company are treated as mentioned in section 273(1) of the Taxes Act 1970 (transfers within a group: no gain/no loss), or
 - (b) an exchange, or a transaction treated for the purposes of section 85(2) and (3) below as an exchange, of shares in or debentures of a company held by company A for shares in or debentures of another company, being a company associated with company A immediately after the transaction, and is treated by virtue of section 85(3) below as a reorganisation of share capital, or
 - (c) a revaluation of an asset in the accounting records of company A.
- In the following conditions the “asset with enhanced value” means (subject to section 26C below), in the paragraph (a) case, the asset acquired by the person to whom the disposal is made, in the paragraph (b) case, the shares in or debentures of the other company and, in the paragraph (c) case, the revalued asset.
- (7) The second condition is that—
- (a) during the period beginning with the transaction referred to in subsection (6) above and ending immediately before the section 26 disposal, there is no disposal of the asset with enhanced value to any person, other than a disposal falling within section 273(1) of the Taxes Act 1970, and
 - (b) no disposal of the asset with enhanced value is treated as having occurred during that period by virtue of section 278 of the Taxes Act 1970 (company ceasing to be member of group).
- (8) The third condition is that, immediately after the section 26 disposal, the asset with enhanced value is owned by a person other than the company making that disposal or a company associated with it.
- (9) The conditions in subsections (6) to (8) above are not satisfied if—

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- (a) at the time of the transaction referred to in subsection (6) above, company A carries on a trade and a profit on a disposal of the asset with enhanced value would form part of the trading profits, or
 - (b) by reason of the nature of the asset with enhanced value, a disposal of it could give rise neither to a chargeable gain nor to an allowable loss, or
 - (c) immediately before the section 26 disposal, the company owning the asset with enhanced value carries on a trade and a profit on a disposal of the asset would form part of the trading profits.
- (10) The amount of chargeable profits of a company to be attributed to any distribution made by the company at any time in respect of any class of shares, securities or rights shall be ascertained by—
- (a) determining the total of distributable profits, and the total of chargeable profits, that remains after allowing for earlier distributions made in respect of that or any other class of shares, securities or rights, and for distributions made at or to be made after that time in respect of other classes of shares, securities or rights, and
 - (b) attributing first to that distribution distributable profits other than chargeable profits.
- (11) The amount of chargeable profits of a company to be attributed to any part of a distribution made at any time to which a person is entitled by virtue of any part of his holding of any class of shares, securities or rights, shall be such proportion of the chargeable profits as are attributable under subsection (10) above to the distributions made at that time in respect of that class as corresponds to that part of his holding.

26B Value shifting: disposals within a group followed by a disposal of shares

- (1) The references in section 26 above to a reduction in the value of an asset, in the case mentioned in subsection (7) of that section, do not include a reduction attributable to the disposal of any asset (“the underlying asset”) by the second company at a time when it and the first company are associated, being a disposal falling within section 273(1) of the Taxes Act 1970 (transfers within group: no gain/no loss), except in a case within subsection (2) below.
- (2) A case is within this subsection if the amount or value of the actual consideration for the disposal of the underlying asset—
- (a) is less than the market value of the underlying asset, and
 - (b) is less than the cost of the underlying asset,
- unless the disposal is effected for bona fide commercial reasons and does not form part of a scheme or arrangements of which the main purpose, or one of the main purposes, is avoidance of liability to corporation tax.
- (3) For the purposes of subsection (2) above, the cost of an asset owned by a company is the aggregate of—
- (a) any capital expenditure incurred by the company in acquiring or providing the asset, and
 - (b) any other capital expenditure incurred by the company in respect of the asset while owned by that company.

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- (4) For the purposes of this section, where the disposal of the underlying asset is a part disposal, the reference in subsection (2)(a) above to the market value of the underlying asset is to the market value of the asset acquired by the person to whom the disposal is made and the amounts to be attributed to the underlying asset under paragraphs (a) and (b) of subsection (3) above shall be reduced to the appropriate proportion of those amounts, that is—
- (a) the proportion of capital expenditure in respect of the underlying asset properly attributed in the accounting records of the company to the asset acquired by the person to whom the disposal is made, or
 - (b) where paragraph (a) above does not apply, such proportion as appears to the inspector, or on appeal the Commissioners concerned, to be just and reasonable.
- (5) Where by virtue of a distribution in the course of dissolving or winding up the second company the first company is treated as disposing of an interest in the principal asset, the exception mentioned in subsection (1) above does not apply.

26C Value shifting: supplementary

- (1) For the purposes of sections 26(1A) and 26A(7) to (9) above, subsections (2) to (6) below apply for the purpose of determining in the case of any asset (“the original asset”) whether it is subsequently disposed of or treated as disposed of or owned or any other condition is satisfied in respect of it.
- (2) References in sections 26(1A)(a) and (b) and 26A(7) to a disposal are to a disposal other than a part disposal.
- (3) References to an asset are to the original asset or, where at a later time one or more assets are treated by virtue of subsections (5) or (6) below as the same as the original asset—
- (a) if no disposal falling within paragraph (a) or (b) of section 26(1A) or, as the case may be, of 26A(7) has occurred, those references are to the asset so treated or, as the case may be, all the assets so treated, and
 - (b) in any other case, those references are to an asset or, as the case may be, all the assets representing that part of the value of the original asset that remains after allowing for earlier disposals falling within the paragraphs concerned,
- references in this subsection to a disposal including a disposal which would fall within the paragraphs concerned but for subsection (2) above.
- (4) Where by virtue of subsection (3) above those references are to two or more assets—
- (a) those assets shall be treated as if they were a single asset,
 - (b) any disposal of any one of them is to be treated as a part disposal, and
 - (c) the reference in section 26(1A) to the asset owned at the time of the disposal by a company associated with the disposing company and the reference in section 26A(8) to the asset with enhanced value is to all or any of those assets.
- (5) Where there is a part disposal of an asset, that asset and the asset acquired by the person to whom the disposal is made are to be treated as the same.

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- (6) Where the value of an asset is derived from any other asset in the ownership of the same or an associated company, in a case where assets have been merged or divided or have changed their nature or rights or interests in or over assets have been created or extinguished, the first asset is to be treated as the same as the second.
- (7) For the purposes of section 26(1A) above, where account is to be taken under that subsection of a reduction in the value of a relevant asset and at the time of the disposal by the disposing company referred to in that subsection—
- (a) references to the relevant asset are by virtue of this section references to two or more assets treated as a single asset, and
 - (b) one or more but not all of those assets are owned by a company associated with the disposing company,
- the amount of the reduction in the value of the relevant asset to be taken into account by virtue of that subsection shall be reduced to such amount as appears to the inspector, or on appeal to the Commissioners concerned, to be just and reasonable.
- (8) For the purposes of section 26A above, where—
- (a) a dividend paid by the second company is attributable to chargeable profits of that company, and
 - (b) the condition in subsection (7), (8) or (9)(c) of that section is satisfied by reference to an asset, or assets treated as a single asset, treated by virtue of subsection (3)(b) above as the same as the asset with enhanced value,
- the amount of the reduction in value of the principal asset shall be reduced to such amount as appears to the inspector, or on appeal to the Commissioners concerned, to be just and reasonable.
- (9) For the purposes of sections 26 to 26B above and this section, companies are associated if they are members of the same group.
- (10) Section 272(1) to (4) of the Taxes Act 1970 (groups of companies: definitions) applies for the purposes of sections 26 to 26B above and this section as it applies for the purposes of that section.”
- (2) This section shall have effect in respect of any disposal of an asset on or after 14th March 1989, but—
- (a) no account shall be taken by virtue of section 26A of the Capital Gains Tax Act 1979 of any reduction in the value of an asset attributable to the payment of a dividend unless it is paid on or after that date, and
 - (b) no account shall be taken by virtue of section 26B of that Act of a reduction in the value of an asset attributable to the disposal of another asset unless the disposal took place on or after that date.