

VENTURE CAPITAL TRUSTS AND CAPITAL GAINS TAX

This Help Sheet explains capital gains aspects of the Venture Capital Trust (VCT) scheme for investors. But it is only an introduction. If you are in any doubt about your circumstances you should ask your tax adviser. Your Inland Revenue office will also be pleased to help and will provide any forms you may require. You can also consult the Inland Revenue Capital Gains Manual, which explains the rules in more detail. The Manual is available on the Inland Revenue website at www.inlandrevenue.gov.uk or you can ask to see it at your local Inland Revenue Enquiry Centre.

This Help Sheet will help you fill in the Capital Gains Pages of your Return.

A VCT is a company which invests in small unquoted companies. Leaflet *IR169: Venture Capital Trusts (VCTs) A brief guide* gives more information. This is available from the Orderline and is on the Inland Revenue website. The VCT shares which qualify for the special VCT tax reliefs are ordinary shares in an approved VCT.

There are two Capital Gains Tax reliefs:

- you may not have to pay Capital Gains Tax on any gain you make when you dispose of your VCT shares. (This is called **disposal relief** in this Help Sheet.)
- you may be able to treat gains arising on disposals around the time your VCT shares are issued as postponed to a later year. (This is called **deferral relief** in this Help Sheet.)

This Help Sheet describes:

- disposal relief
- deferral relief
- when the deferred gain is brought back into charge
- how deferral relief fits in with disposal relief
- what happens if the VCT
 - is taken over, or
 - makes a bonus or rights issue.

WHAT IS DISPOSAL RELIEF?

If disposal relief is due, you will not have to pay Capital Gains Tax on any gain you make on the disposal of VCT shares. The following conditions have to be met:

- you did **not** acquire more than £100,000 worth of VCT shares in any one tax year
- you are an individual (not a trustee)
- you are 18 or over at the date of disposal
- the company was an approved VCT both when you acquired the shares and when you dispose of them
- you acquired the shares for commercial reasons and not as part of a tax avoidance scheme.

Any loss you make on the disposal of VCT shares where these conditions are met is not allowable for capital gains purposes.

— **Does it matter how I acquire the VCT shares?**

No. For disposal relief, it does not matter whether you subscribe for newly issued shares or whether you acquire existing shares, for example, by purchase or inheritance.

— **What happens if I dispose of VCT shares when I acquired more than £100,000 worth in any one tax year?**

You will not have to pay Capital Gains Tax on any gain on your disposal of the first £100,000 worth of the shares acquired in any tax year. A gain on your disposal of shares acquired above this limit is chargeable to Capital Gains Tax. Similarly a loss is only allowable if it arises on the disposal of shares acquired above the £100,000 limit. The normal capital gains rules apply to disposals of shares acquired above this £100,000 limit. *Help Sheet IR284: Shares and Capital Gains Tax* explains these rules, and is available from the Orderline and on the Inland Revenue website.

There are identification rules to decide which shares count first towards the £100,000 limit. Shares acquired earlier in the tax year count first. Shares acquired on the same day in different VCTs or in different classes of ordinary shares in the same VCT are identified on a proportionate basis.

— **What happens if I sell some but not all of my VCT shares when I acquired more than £100,000 worth in any one tax year?**

You identify your disposals on a first in - first out basis.

In relation to shares acquired on the same day, shares acquired in excess of the £100,000 limit are treated as disposed of before other shares acquired on that day. This is illustrated in Example 1 on page 2 of this Help Sheet.

— Do I need to disclose any gain arising from a disposal of VCT shares on my Tax Return?

You must give details of the disposal on Pages CG2 and CG3 of the Capital Gains Pages if either the total value of the VCT shares and any other assets you disposed of in the tax year or your total chargeable gains were more than the figures shown on page CGN2 of the Notes on Capital Gains. If, after disposal relief, you do not have to pay Capital Gains Tax on any of the gain, describe the VCT shares in column A on Page CG2, enter the disposal proceeds in column F, enter Nil in column H, write 'VCT disposal relief' in column G and state the amount of relief claimed.

Example 1

You buy 150,000 VCT shares for £150,000 on the same day. 100,000 shares qualify for disposal relief so any gain on the disposal of these 100,000 shares is exempt. Any gain on the remaining 50,000 shares is not exempt.

In the following tax year you sell 75,000 of the 150,000 shares.

You identify the sale of the 75,000 shares as follows:

- the first 50,000 with the 50,000 non exempt shares
- the remaining 25,000 with 25,000 of the shares the gain on whose disposal is exempt.

You calculate any gain or loss on the 50,000 non exempt shares.

Any gain is chargeable to Capital Gains Tax and any loss is allowable. You describe the VCT shares in column A on Page CG2 of the Capital Gains Pages, enter the proceeds from the disposal of the 75,000 shares in column F, any gain or loss arising on the 50,000 non exempt shares in column H, write 'VCT disposal relief' in column G and state the amount of relief claimed.

You still hold 75,000 shares, the gain on whose disposal will be exempt.

WHAT IS DEFERRAL RELIEF?

When you dispose of an asset and make a gain you usually pay Capital Gains Tax for the tax year in which you dispose of the asset. Deferral relief lets you treat the gain as not arising until some future date. If you make a claim and defer a gain, the gain may be charged to Capital Gains Tax in a later tax year, usually when you dispose of the VCT shares.

— Which gains can I defer?

You can claim deferral relief for any gain which arises on your disposal of an asset on or after 6 April 1995. You can also claim deferral relief when a gain, previously deferred under the VCT scheme or the Enterprise Investment Scheme, is 'revived'. (Revived means the gain is brought back into charge to Capital Gains Tax.)

— Which VCT shares qualify?

You can claim deferral relief if you subscribe for VCT shares and receive 'front-end' Income Tax relief on the shares. This Income

Tax relief is described in the notes for box 15.3 on page 21 of the Tax Return Guide and is called 'front-end' Income Tax relief in this Help Sheet to distinguish it from another relief on VCT dividends (see leaflet *IR169: Venture Capital Trusts (VCTs) A brief guide*).

If your VCT shares were issued before the date on which the gain you claim to defer arose, you must still hold them at that date.

— What are the time limits for subscribing for VCT shares to obtain deferral relief?

The VCT shares you subscribe for must be issued to you in the period beginning 12 months before and ending 12 months after the gain arises. The Inland Revenue has discretion to extend these time limits. Your Inland Revenue office can explain the circumstances in which they can do this.

Example 2

You dispose of an asset on 6 June 2001. You can claim deferral relief for a gain on the disposal if you subscribe for VCT shares on which you receive 'front-end' Income Tax relief and these shares are issued to you at any time between 6 June 2000 and 6 June 2002.

— Who can claim deferral relief?

You can claim relief if you are an individual resident or ordinarily resident in the UK. You cannot claim relief if you are treated by double taxation relief arrangements as resident elsewhere, so that (ignoring disposal relief) you would not be liable to UK Capital Gains Tax on any gain from the VCT shares.

— How do I claim deferral relief?

Please complete the form on page 5 of this Help Sheet and attach it to the Capital Gains Pages of your Tax Return. If the gain(s) against which you are claiming deferral relief arose in the tax year to which this Tax Return relates, also write 'VCT deferral relief' in column G on Page CG2 of the Capital Gains Pages next to the relevant disposal(s) and state the amount of relief claimed.

— How much deferral relief can I claim?

You can claim the amount you subscribe up to £100,000 for shares issued in any one tax year.

You may claim less than the maximum deferral relief, for example, if you want to use your annual exempt amount of £7,500 to cover part of your gains.

If you do not receive 'front-end' Income Tax relief in full because your Income Tax liability is insufficient, then, provided you receive some 'front-end' Income Tax relief, you can still claim to defer gains up to the full amount you subscribe for VCT shares, subject to the £100,000 limit for shares issued in any tax year.

Example 3

In one tax year:

- your Income Tax liability is £12,000 before 'front-end' Income Tax relief,
- you have a gain of £100,000 on a disposal, **and**
- you subscribe £100,000 for 100,000 VCT shares issued to you in the same tax year.

Your 'front-end' Income Tax relief is restricted to £12,000. The annual exempt amount for the tax year is £7,500. You can claim deferral relief on the full subscription of £100,000 or on any smaller amount, for example, £92,500, leaving £7,500 to be covered by your annual exempt amount.

If your Income Tax liability is nil before taking account of your subscription for VCT shares, you will receive no 'front-end' Income Tax relief for your subscription. In this case you cannot claim any deferral relief.

You can defer gains of more than £100,000 arising in any one tax year by making subscriptions for shares issued in different tax years.

Example 4

You subscribe £100,000 for VCT shares which are issued on 4 April 2001. You still hold these shares when you sell an asset realising a gain of £400,000 on 1 April 2002. You make further subscriptions:

- £100,000, VCT shares issued on 1 April 2002
- £100,000, VCT shares issued on 31 March 2003.

You send your Tax Return for 2001-02 during January 2003. Provided you received 'front-end' Income Tax relief on all the VCT shares already issued, you can claim 2000-01 deferral relief of £100,000 and 2001-02 deferral relief of £100,000 against your gain on your Tax Return for 2001-02. This leaves £200,000 chargeable in 2001-02. Capital Gains Tax due will be payable on 31 January 2003.

Provided you receive 'front-end' Income Tax relief for all the shares issued on 31 March 2003, you can claim deferral relief on a further £100,000 of the gain for 2002-03. Part of the Capital Gains Tax paid will be refunded, leaving £100,000 gains chargeable in 2001-02.

— What is the time limit for claiming deferral relief?

You can make a claim to deferral relief up to five years from 31 January in the year following the tax year in which:

- the gain to be deferred arose, **or**
- your VCT shares were issued

whichever is the later.

WHEN IS THE DEFERRED GAIN REVIVED?

Usually this will be in the tax year when you dispose of the VCT shares (unless the disposal is to your husband or wife at no gain/no loss for capital gains purposes, in which case it will be when that person disposes of them).

The deferred gain would be revived earlier than this if:

- you (or your husband or wife to whom you have transferred your shares) cease to be resident in the UK, if this happens within three years (five years if the VCT shares were acquired before 6 April 2000) from the time the shares were issued. But this does not apply if whichever of you holds the shares takes up employment outside the UK and becomes resident again within three years without disposing of any of the shares in the meantime
- the company loses Inland Revenue approval as a VCT
- any of the 'front-end' Income Tax relief on your VCT shares is withdrawn in other circumstances
- there is a share exchange or company reconstruction which is not treated as a disposal, and the new assets held following the exchange or reconstruction are not ordinary shares in a VCT.

The deferred gain will not be revived if you die.

— How do I return the deferred gain when it is revived?

You must give details on Pages CG2 and CG3 of the Capital Gains Pages. Please enter 'VCT deferral relief: gain revived' in column A and in column H the amount of the revived gain.

You can use your annual exempt amount, £7,500 for 2001-02, for the tax year in which the deferred gain is revived to cover the whole or part of the revived gain.

— How much of the deferred gain is revived?

The whole of any deferred gain is revived if :

- you dispose of all your VCT shares, see Example 5 below, **or**
- the event giving rise to the revived gain is not a disposal of your VCT shares (for example, if, within three years from the time the shares were issued, you emigrate, intending to stay outside the UK permanently).

Example 5**This deals only with the revived gain.**

You defer a gain of £50,000 on a disposal in 2001-02 by subscribing for £50,000 worth of VCT shares issued in 2001-02. If you sell all the VCT shares in 2002-03, the deferred gain of £50,000 is revived in 2002-03.

If you dispose of only some of your shares, some of the deferred gain will be revived.

Example 6**This deals only with the revived gain.**

You defer a gain of £20,000 arising in 2000-01 by subscribing for £20,000 worth of VCT shares issued in 2000-01. If you sell 15,000 VCT shares in 2001-02, part of the deferred gain is revived in the tax year 2001-02. All your VCT shares were used to defer the gain and, as you have sold 15,000 out of the 20,000 shares, the same proportion of the deferred gain is revived: £15,000.

The position is more complicated where you only dispose of some of your shares and you claimed deferral relief on some, but not all, of these shares. You have to identify the shares you have disposed of and the shares which have had deferral relief.

— What are the identification rules?

You identify disposals on a first in - first out basis.

When shares were acquired on the same day, you identify disposals first against shares which have not been used in the claim for deferral relief.

— How does deferral relief fit in with disposal relief?

Subscriptions for shares which are used in claims for deferral relief may also count towards the £100,000 on which disposal relief is available.

Example 7

You sell an asset realising a gain of £60,000. You subscribe £100,000 for 100,000 shares in a VCT which are issued to you in the same tax year. You receive deferral relief against the gain of £60,000. In a subsequent tax year you sell 55,000 of the VCT shares.

The 100,000 VCT shares are the only VCT shares you acquired in the tax year and therefore they all qualify for disposal relief, so that any gain you make on the sale of the 55,000 VCT shares is not chargeable to Capital Gains Tax.

Only £60,000 of the subscription is used in the claim for deferral relief.

Therefore £40,000 expenditure on 40,000 shares has not attracted deferral relief.

The 55,000 shares sold are identified as follows:

- first, against 40,000 shares for which no deferral relief was given
- second, against 15,000 shares for which deferral relief was given.

Deferral relief was given in respect of 60,000 shares of which 15,000 were sold, so the proportion of the £60,000 deferred gain to be revived is $\frac{15,000}{60,000} = £15,000$.

£15,000 of the deferred gain is revived in the tax year in which you sell the 55,000 VCT shares.

WHAT HAPPENS IF ANOTHER COMPANY TAKES OVER THE VCT?

The VCT or the other company involved usually writes to you explaining the tax implications.

For capital gains purposes you are not treated as disposing of your VCT shares if another VCT takes over the VCT in which you hold shares and just issues new VCT ordinary shares to you. In these circumstances, and provided any 'front-end' Income Tax relief is not withdrawn, VCT deferral relief continues.

With all other take-overs:

- you are treated as disposing of any VCT shares which qualify for exemption on disposal
- any deferred gain will be revived.

WHAT HAPPENS IF THE VCT MAKES A BONUS ISSUE OF SHARES?

For capital gains purposes, the original shares and the bonus shares related to them are treated as the same asset. This means that if you deferred a gain, your deferral relief continues and is apportioned between the original and the bonus shares.

WHAT HAPPENS IF THE VCT MAKES A RIGHTS ISSUE OF SHARES?

If you subscribe for the rights shares, this is usually treated as a separate subscription for capital gains purposes and will qualify for the Capital Gains Tax reliefs if the relevant conditions are met.

Any deferral relief you have received continues but relates only to the shares on which it was originally given.

These notes are for guidance only, and reflect the position at the time of writing. They do not affect any rights of appeal.

Claim for Venture Capital Trust Capital Gains Tax deferral relief

Name	Tax reference
<input type="text"/>	<input type="text"/>

VCT shares

Description of shares and name of company	Date shares issued to you	Cost	Deferral relief to be set against gain
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
Total amount of deferral relief			£ <input type="text"/>

Assets you disposed of

Description	Date of disposal	Chargeable gain	Gain to be deferred
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>
<input type="text"/>	<input type="text" value="/ /"/>	£ <input type="text"/>	£ <input type="text"/>

If more than one block of shares was issued to you or you made more than one gain, make clear how each block of shares used in your claim for deferral relief fits in with the gain(s) to be deferred.

I claim relief as detailed above. The particulars given in this claim are correctly stated to the best of my information and belief.

Signature

Date