



FIELD COURT TAX CHAMBERS

McQuillan and ordinary share capital¹

The taxpayer is denied entrepreneurs' relief

The case of *McQuillan v HMRC* [2017] UKUT 344 (reported in *Tax Journal*, 15 September 2017) gave rise to a very interesting (or rather, extraordinary) issue. It concerned the entitlement to entrepreneurs' relief and whether the 5% shareholding requirement was satisfied.

Mr and Mrs McQuillan each held 33% of the (full strength) ordinary shares in a trading company. Some other shareholders had 30,000 non-voting shares which had no rights to dividends.

The problem was that if the 30,000 non-voting shares were 'ordinary shares' for the purposes of entrepreneurs' relief, the taxpayers would obviously not have the necessary 5% of the ordinary share capital and would therefore not qualify for the relief.

The definition of ordinary share capital for this purpose is found in ITA 2007 s 989 and provides as follows:

“all the company's issued share capital (however described), other than capital the holders of which have a right to a dividend at a fixed rate but have no other right to share in the company's profits”.

The non-voting shares were obviously part of the issued share capital and could only be disregarded if they had a right to a dividend at a fixed rate. The First-tier Tribunal (FTT) therefore had to decide whether having no rights to a dividend was the same as having a right to a dividend at a fixed rate; i.e. a rate of 0%.

HMRC argued that the shares did not have a right to a dividend at a fixed rate – they did not have a right to a dividend at all – and could not therefore be excluded from the definition of ordinary share capital. The fact that this gave rise to a grotesquely unfair result which could not possibly have been intended by Parliament (does this resonate with anybody?) made no difference.

It seemed to me that the taxpayer had a really difficult argument. How can the absence of a right really be described as a right at 0%? For example, if I buy a car, this would obviously not give me the right to a refund of my TV licence fee. However, nobody in their right mind would say that the purchase of the car gives me 'a right to a TV licence refund at a rate of 0%'.

However, the FTT was clearly seized by the need for justice and fairness. It found that in these circumstances the absence of a right to a dividend was equivalent to a right to a dividend at a

¹ This article was first published in the InBrief section of *Tax Journal* published by LexisNexis on 3rd November 2017

fixed rate and allowed the relief. Obviously, this was a triumph for common sense (and fairness) even if the analysis was difficult to follow.

The matter might have simply been left there (perhaps pursuant to a need for fairness and justice)..... but regrettably not. HMRC appealed to the Upper Tribunal who concluded that having no right to a dividend cannot be regarded as a right to a dividend at a rate of 0%. The Upper Tribunal were really sympathetic and tried its best, but it could find no construction (purposive or otherwise) that could prevent these shares from being ordinary share capital within the definition in s 989. It recognised that this was just the sort of case for which entrepreneurs' relief was devised and that this interpretation appeared unfair, but found it impossible to conclude that Mr and Mrs McQuillan were entitled to entrepreneurs' relief.

I wonder if there should be a campaign for a 'reverse GAAR'.

Peter Vaines

Field Court Tax Chambers