14 September 2026

Modernising the taxation of distributions and repayments of capital from companies

Comments from Saffery LLP

1. Executive summary

1.1 We welcome the opportunity to comment on the proposals to modernise the taxation of distributions and repayments of capital from companies.

1.2 In summary, our key points are as follows:

- Existing legislation and HMRC's compliance powers should be used before introducing further rules that would add complexity.
- Removing the ability to undertake capital reduction demergers is unlikely to increase use of the statutory regime as businesses may instead revert to section 110 demergers.
- We welcome relaxing the statutory demerger conditions.
- Any reforms affecting non-UK companies must respect foreign corporate and tax law while ensuring fair treatment compared with distributions from UK companies.
- Existing case law has developed principles for addressing differences between UK tax concepts and foreign company law.
- The proposed changes to non-UK distributions could create significant reporting challenges for banks, investment platforms and portfolio investors.
- HMRC should use its existing powers to determine whether loans from non-UK companies are genuine rather than introducing a new temporary tax regime.
- A broader commercial benefit test would be preferable to the proposed mechanical conditions for purchases of own shares.
- Any reform of the TIS rules should not widen their scope and should operate through self-assessment.

1.3 Section 2 below makes some general comments on the proposals, and section 3 covers our responses to the specific questions raised in the consultation document.

1.4 We would be happy to discuss the points raised here in further detail. If you have any questions, or would like any further information, please contact: Sean McGinness, National Tax Partner, on +44 (0)131 221 3217 or email sean.mcginness@saffery.com or Ami Jack, Partner, National Tax, on +44 (0)330 094 3079 or email ami.jack@saffery.com.

2. General points

2.1 It is important that any reforms both respect and work with foreign corporate and tax law while ensuring fair treatment compared with distributions from UK companies. Foreign legal concepts do not always map directly onto UK tax concepts and any changes should recognise those differences.

3. Specific consultation questions

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

3.1.1 Any proposals that make it more difficult to restructure corporate groups will have an impact on corporation tax payers.

3.2 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?

3.2.1 We are not convinced that new rules are required to address the planning described in the consultation. In our view, arrangements which seek to secure capital gains tax treatment without changing the shareholder's underlying equity interest are already at risk of counteraction under the Transactions in Securities (TIS) rules.

3.2.2 If HMRC wishes to counteract this type of planning, it should enforce the existing TIS rules. Consideration could also be given to bringing those rules within self-assessment.

3.2.3 Introducing further rules instead of applying the existing legislation would just add complexity.

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

3.3.1 No comment.

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

3.4.1 The proposal could create divergence between the accounting and tax treatment of share capital, potentially requiring separate records to be maintained.

3.4.2 Consideration should also be given to any deferred tax implications arising from that divergence.

3.4.3 The consultation proposes changes which are intended to increase reliance on the statutory demerger regime. At the same time, it proposes removing the existing right to an automatic tribunal appeal where statutory demerger clearance is refused. Such a change would reduce procedural safeguards for taxpayers as greater reliance is placed on the statutory route.

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

3.5.1 We would currently recommend a non-statutory demerger where the conditions for statutory demerger relief cannot be satisfied. In particular, the statutory route may not be feasible where there are insufficient distributable reserves, or where the trading condition is not satisfied.

3.5.2 Removing the ability to undertake a capital reduction demerger is unlikely to result in all transactions moving to the statutory demerger regime. Businesses are likely instead to revert to using demergers under section 110 Insolvency Act 1986, where the process and tax analysis are largely the same as under the current capital reduction demerger route. However, this may involve additional liquidator fees, increased complexity and another set of professional advisers. Some taxpayers may also be concerned about the association with placing a company into liquidation.

3.5.3 Although in principle a statutory demerger is more straightforward, we would also recommend a non-statutory demerger where the conditions in Condition D make the statutory route unattractive. The non-statutory clearance process allows each transaction to be considered on its own facts. This may include situations where a demerger is intended to facilitate a sale.

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

3.6.1 Yes. We welcome the proposal to relax the conditions for statutory demergers.

3.6.2 In practice, statutory demergers are rarely used because one or more of the conditions cannot be met. The trading condition is a common barrier, as many demergers involve separating investment assets from trading activities.

3.6.3 Relaxing the conditions would enable statutory demerger relief to be used more widely and give advisers and taxpayers greater certainty over the tax treatment, as the statutory clearance process provides confirmation that the conditions for relief are satisfied.

3.6.4 The legal paperwork for a statutory demerger can also be more straightforward, as there is no need to create a new holding company, and the process may be easier for taxpayers to understand.

3.6.5 There may also be cost savings where a valuation is not required. However, a valuation may still be needed for a partition demerger to manage the risk of a transfer of value.

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

3.7.1 We question why Condition F (which requires the distributing company to remain a trading company or the holding company of a trading group following the demerger, except in specific circumstances involving 75% subsidiaries) is not also being removed.

3.7.2 If Condition C is removed, a new bona fide commercial condition will be needed. The difficulty with the existing Condition C is that it requires a benefit to the trade, rather than a benefit to the shareholders or company more generally.

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

3.8.1 No comment.

3.9 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?

3.9.1 This question presupposes that capital reduction demergers will be removed. As noted in our response to question 2, we are not convinced that this is necessary, as arrangements of the type described in the consultation are already at risk of counteraction under the TIS rules.

3.9.2 Even if capital reduction demergers were removed, businesses are likely to revert to using section 110 demergers rather than move to the statutory demerger regime.

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

3.10.1 No comment.

3.11 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?

3.11.1 The case law in this area arose precisely because it is not always possible to map foreign legal concepts directly into UK tax law (see also our response to Question 18).

3.11.2 We would be concerned that there would continue to be situations where the terms of the distribution do not clearly fall within the wording of the legislation, and case law and interpretation would still be required.

3.11.3 If this proposed reform is intended to tax a wider category of distribution then the government should be transparent on this, rather than presenting the proposal as one which will reduce uncertainty.

3.12 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?

3.12.1 No comment.

3.13 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.

3.13.1 The proposed change would have a significant impact on reporting by banks and other investment platforms.

3.13.2 Systems used to prepare tax reporting packs would need to be updated because the treatment of corporate actions would need to be recoded. This process could take several years.

3.13.3 HMRC should anticipate that, during the transition, many portfolio investors may not receive tax reports which reflect the new treatment correctly.

3.14 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?

3.14.1 No comment.

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

3.15.1 No comment.

3.16 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?

3.16.1 No comment.

3.17 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?

3.17.1 Examples include profit participating loans and loans which are not made on arm's length terms.

3.17.2 Receipts from those arrangements are taxed as interest but would be taxed as distributions under the proposed changes.

3.17.3 The main effect of the distributions rules is to disallow a deduction for the payer, which would not be relevant where the payer is non-UK resident.

3.18 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?

3.18.1 There is already an established body of case law dealing with the interaction between UK distributions legislation and foreign company law concepts.

3.18.2 For example, First Nationwide v HMRC [2012] EWCA Civ 278 established that the foreign law mechanism by which a payment is made is central to determining its UK tax treatment. Buckingham v HMRC [2023] UKFTT 358 demonstrated the practical difficulties that can arise in determining whether a distribution from a non-UK company should be treated as income or capital, including situations where a single payment may contain both elements. More recently, Beard v HMRC [2025] EWCA Civ 385 confirmed that distributions from a Jersey company paid from a share premium account were not dividends of a capital nature and reinforced the importance of the underlying foreign law mechanism rather than the label attached to the reserve from which the payment was made.

3.18.3 These cases illustrate the practical tensions that can arise where foreign company law concepts do not map neatly onto UK tax concepts, particularly in relation to dividends of a capital nature, repayments of capital and distributions made from share premium or similar reserves.

3.18.4 Given that the courts have already developed principles for addressing these issues, it is not clear that further legislation is required. If legislation is introduced, it should clearly identify what issues are not adequately addressed under the existing case law and ensure that the principles developed by the courts are not inadvertently disturbed.

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

3.19.1 No comment.

3.20 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?

3.20.1 The existing case law already provides useful insight into the difficulties that can arise when determining whether a distribution from a non-UK incorporated company should be treated as a dividend.

3.20.2 Cases such as First Nationwide, Buckingham and Beard demonstrate that the UK tax treatment of a payment can depend heavily on the legal mechanism by which it is made under the relevant foreign law, the character of the reserve or fund from which it is paid, and the extent to which the foreign law concept corresponds with established UK tax principles.

3.20.3 Difficulties may also arise where foreign company law permits transactions that do not have a straightforward equivalent under UK company law. This may include gifts to shareholders, transfers at undervalue, or gifts and transfers to related or unrelated companies.

3.20.4 For example, a company incorporated in the British Virgin Islands may be able to transfer an asset at undervalue to an unrelated company. An equivalent transaction by a UK company would be ultra vires, but would not necessarily be treated as a dividend. Any clarification of the rules would therefore need to address how such transactions should be characterised.

3.20.5 If legislation is introduced, it should accommodate transactions which are valid under the relevant foreign company law but do not have a direct equivalent under UK law.

3.21 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 any difficulties with calculating the nominal value of the share in some jurisdictions?

3.21.1 The use of nominal value should be permissive rather than mandatory.

3.21.2 Many jurisdictions allow capital contributions which are not reflected in the nominal value of the shares. Any legislation would need to address those circumstances.

3.21.3 For example, in many jurisdictions it is possible to make capital contributions without increasing the nominal value of the shares. This illustrates the difficulties that can arise where foreign company law concepts do not map neatly onto UK concepts of share capital.

3.21.4 Consideration should also be given to allowing shareholders to rely on information provided on a Schedule K-1 for a US company.

3.22 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?

3.22.1 No comment.

3.23 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?

3.23.1 It is not always clear when a distribution may be unlawful. This may arise because of genuine uncertainty or a lack of awareness of the relevant company law requirements.

3.23.2 Any priority rule would therefore need sufficient flexibility to deal appropriately with the circumstances of each case.

3.24 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?

3.24.1 No comment.

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

3.25.1 No comment.

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

3.26.1 We consider that these issues should be addressed through guidance.

3.26.2 There is well-established company law concerning unlawful distributions. Introducing a different characterisation for tax purposes would create confusion.

3.26.3 The tax treatment should instead follow the characterisation of the payment under company law.

3.27 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.

3.27.1 The proposal would create administrative difficulties for taxpayers who are not currently within self-assessment, as they may be required to file a tax return solely because they have received a relevant loan.

3.27.2 The rules would also need to address individuals who become or cease to be UK resident while a loan is outstanding.

3.27.3 We do not agree that taxpayers are already required to determine whether a non-UK resident company would be close for the purposes of the TIS rules. Those rules are not within self-assessment and HMRC must establish whether they apply.

3.28 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?

3.28.1 Loans are not economically the same as distributions because there is an obligation to repay them.

3.28.2 If HMRC is concerned that distributions are being presented as loans, it should use its existing powers to establish whether the arrangements are genuine loans, including whether there is an intention to repay.

3.28.3 Where a purported loan is not a genuine loan, the amount will already be taxable under existing legislation. In our view, HMRC should apply the existing legislation and compliance powers rather than introducing a new temporary tax regime.

3.29 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?

3.29.1 Of the four options, option 3 would be the only potential acceptable option. However, subject to an analysis of the relevant foreign law, we would often expect the write-off of a loan to be treated as a distribution under existing law.

3.29.2 We strongly oppose the other options.

3.29.3 In relation to option 4, treating a loan as a distribution simply because it remains outstanding for three or five years would not reflect the commercial reality of many loan arrangements.

3.29.4 For example, a loan may be made by a foreign private equity-owned holding company to facilitate a transaction. The loan may be genuinely repayable but remain outstanding for more than five years because of the investment profile.

3.30 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?

3.30.1 Whether a company is close is not always clear. Applying the close company definition to a foreign company would create additional complexity.

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

3.31.1 This point is not applicable because the existing s455 rules apply to loans generally rather than only to loans which are non-commercial. Such loans would be taxed under the proposals, which we oppose for the reasons outlined above.

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

3.32.1 A material interest threshold would not address the underlying issue. As explained in our response to Question 28, HMRC should instead use its existing powers to determine whether a loan is genuine.

3.33 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?

3.33.1 Notwithstanding any exclusions for loans made in the ordinary course of business, we believe that any new rules should include appropriate grandfathering provisions for existing loans.

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

3.34.1 Rather than replacing the trade benefit test with the proposed mechanical conditions, the government should consider introducing a broader commercial benefit test. This would allow sufficient flexibility to take account of the circumstances of each transaction.

3.34.2 The proposed conditions would represent a significant narrowing of the existing relief and some of the thresholds appear arbitrary.

3.34.3 For example, it is unclear why a shareholder with a 4% interest should be excluded from relief. If anything, the scope for abuse may be lower where the shareholder has only a small interest.

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

3.35.1 No comment.

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

3.36.1 We have no objection in principle to updating the TIS rules. However, the scope of the rules should not be widened.

3.36.2 The existing rules have been updated over time to reflect market practice and should provide a clear starting point for any reform.

3.36.3 Any new rules should operate through self-assessment rather than depending on an HMRC assessment.

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

3.37.1 The introduction of new rules may encourage taxpayers to accelerate transactions before those rules take effect.

3.37.2 New legislation and uncertainty over its interpretation may also lead to an increase in applications for non-statutory clearance.

3.37.3 If a new statutory clearance procedure is introduced, consideration should be given to whether it could cover the wider conditions for the relief rather than being limited to the commercial purpose test.

4. About Saffery LLP

4.1 At Saffery, we’re more than just chartered accountants and tax and business advisers. We’re a partner-led and people-focused firm, committed to our clients and honouring our heritage.

4.2 Since 1855, we’ve evolved in size and scope, but our unwavering dedication to exceptional client service remains the same.

4.3 As a proud member of Nexia, a worldwide network of trusted member firms, we've got access to local insight on a global scale.

4.4 In the UK, Saffery LLP is the 15th largest accountancy firm by fee income, with 90+ partners and 1,300+ staff across nine offices. Saffery also has an office in Dublin, Ireland.