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Modernising UK stamp duty: are we nearly there yet?

*The UK tax authority (HM Revenue & Customs (**HMRC**)) has published a consultation for a new UK stamp tax on securities regime. It is proposed that the existing stamp duty and stamp duty reserve tax (**SDRT**) legislation will be rewritten, modernised and consolidated. The new tax is proposed to be self-assessed and administered in line with the rest of the UK tax system and will be subject to clear rules on geographical scope, tax base and calculation of liability. The majority of the proposals are sensible and will be a welcome simplification. The 1.5% charge on the issuance or transfer of securities into a clearance system is not covered and its future remains uncertain.*

Stamp duty modernisation – a long and winding road

Following on from the Office for Tax Simplification (***OTS***) report in 2017, and a Call for Evidence issued by HMRC in 2020, a joint HMRC and industry working group has been developing a blueprint for a new UK stamp tax on securities regime which was reflected in an HMRC consultation published on 27 April 2023.

If implemented, the changes proposed would be a significant consolidation, modernisation and simplification of a regime which is plainly out of step with modern business practices. Six years after the OTS said there was an '*urgent case for modernisation*', these changes are long overdue.

If this really is to be the end of stamp duty as we know it, then it would be remiss not to set the scene with some stamp duty trivia. Stamp duty was first introduced in England in 1694 to fund the wars against France. At its peak, it covered a wide range of transactions (including newspapers, lottery tickets, hats, gloves, hair powder, adverts, perfumes and insurance policies). It started life as a fixed duty per transaction and then later became an *ad valorem* tax in the early 19th century. But its scope has been significantly curtailed over time. Key milestones include the introduction of SDRT for on-market securities transactions in 1986, and the introduction of stamp duty land tax (***SDLT***) for transfers of land in 2003. Most recently, an electronic stamping process was introduced in 2020 in response to the Covid-19 pandemic – following which the Victorian stamping machines that, incredibly, had remained in use were retired.

Since 1986 the UK has therefore had two parallel taxation regimes for transactions involving equity securities (with some residual application to debt securities). Stamp duty proper is now generally only paid on the off-market transfer of shares in UK incorporated companies. As noted above, SDRT is typically paid in relation to on-market securities transactions. However, the interaction between these two regimes is not always straightforward – they take different approaches on fundamental matters such as defining the tax point, the nature of in-scope securities, the required UK nexus and even the amount of consideration on which the tax is charged. The rules which are intended to ensure that payment of stamp duty franks any associated SDRT charge (thereby avoiding double taxation of a single transaction) are also relatively strict and need to be considered carefully in a range of common commercial scenarios. Compounding these difficulties, the legislation for stamp duty in particular is very hard to access, being scattered across a series of Acts dating back to the 19th century with no clear signposting or common drafting approach.

These issues aside, stamp duty and SDRT are an important revenue raiser for the government, together raising £4.37bn in FY 21/22. It is clearly appropriate for such an important source of revenue to be backed by a clear and modern legislative framework: enter the current consultation, in which HMRC proposes to introduce a single tax on securities (an ***STS***) to replace the current antiquated and fragmented legislative framework.

It is proposed that the new STS will replace and consolidate the existing stamp duty and SDRT rules, eliminating the various difficulties in navigating between the two regimes whilst seeking to retain the key features of the SDRT

regime for listed securities in order to prevent unnecessary disruption to the operation of the CREST system. It is proposed to be a self-assessed tax, administered in line with the rest of the UK tax system, and will be subject to clear rules on geographical scope, tax base and calculation of liability.

The majority of the proposals are sensible and will be a welcome simplification of a complex regime.

A self-assessment regime

The move to electronic stamping in 2020 was a welcome development, doing away with the requirement for original stock transfer forms to be physically submitted to the Stamp Office (with the associated risk of them being lost or misplaced in transit).

But inefficiencies remain. The Stamp Office must still consider each application for stamping or adjudication, confirm the amount of any liability, track down the payment in its bank account and issue evidence that the tax has been paid. HMRC recommends that customers allow 20 working days for stock transfer forms to be processed, but some applications (in particular, relief applications) can take significantly longer. All the while, the company registrar is unable to update the register of members to reflect the transaction in question.

An administratively simpler future awaits. STS will be a self-assessed tax for which the buyer of the securities will be liable. For off-market transactions, the process will be digitised for the first time using a new HMRC online portal. No change is expected to the mechanics by which SDRT is currently accounted for through CREST, in order to avoid disruption to existing systems.

It will still be important to pay STS in order to update the company share register, but the process will be streamlined. The online portal is intended to give the ability to input the transaction, claim relief or pay STS and immediately receive a Unique Transaction Reference Number (***UTRN***). Registrars will be entitled to update company registers upon receiving that UTRN thereby enabling same day registration. The complex structures involving declarations of trust that are sometimes adopted to allow same-day updating of the register can be consigned to the history books.

It is hoped that the new approach will also eliminate the need for HMRC to confirm whether a court order sanctioning a transfer scheme attracts stamp duty before Companies House will accept the order and give effect to the scheme.

It is proposed that the charging point will be the date of agreement, or the date on which a conditional agreement becomes unconditional, with an overall two-year time limit. The accountable date will be 14 days from the charging point. This proposed deadline deserves further thought: it is not at all uncommon in acquisitions of private companies for a transaction to close at a month end, which may well be more than 14 days after the agreement goes unconditional. It will be cumbersome to have to provide for a separate flow of funds to meet the STS cost and it may be that the issue could be substantially removed by a longer time limit (perhaps 60 days) or by tying the time limit to completion of the transaction (with a longstop to prevent 'resting on contract' planning).

HMRC is not minded to provide for a statutory pre-clearance process. They note that the certainty provided by the current adjudication process only takes place after the transaction and that a statutory pre-clearance system would be inconsistent with the way that HMRC treats other self-assessed taxes. Non-statutory clearance will, however, continue to be available.

The SDRT enforcement regime (including in relation to assessment times, discovery and information / inspection powers, interest and penalties) would be adopted for STS. However, a mitigation of the current rules is proposed for a 'first time' offender, which is welcome given the potential under the current rules for an inadvertent mistake to result in the accumulation of substantial penalties before the error is discovered.

Scope

Geographical scope

The geographical scope of stamp duty is a particular pinch point of the current regime. In practice, no one (including, according to the consultation document, HMRC) expects stamp duty to be paid on the transfers of shares in non-UK incorporated companies. But you won't find that principle set out in the legislation.

This is the *de facto* position because there is no legal obligation on a buyer to send an instrument of transfer for stamping. A buyer will therefore generally only do so in order to ensure (a) that the share register can be updated without triggering a £300 penalty for the registrar and (b) that SDRT will not become payable.

So far so (sort of) straightforward. But pity the advisors who then need to explain to their clients the effect of section 14(4) Stamp Act 1891, which precludes unstamped instruments of transfer from being adduced as evidence in an English court if they relate to property situate in the UK, have been executed in the UK or relate to a matter or thing done or to be done in the UK. Cue the lengthy debate as to whether it is really necessary to execute a transfer of non-UK shares offshore (which is ineffective in taking the transaction outside of section 14(4) if it will nevertheless involve a matter or thing done in the UK) and whether it really matters if the instrument of transfer is not required as evidence anyway (for example, if the register once updated is determinative of ownership). If the proposals in

the consultation paper are taken forward then such debates should be a thing of the past.

It is proposed that the SDRT geographical scope rules are adopted instead, narrowing the scope of the charge to transactions involving securities issued by UK bodies corporate (with certain limited extensions). Further clarity on the intended treatment of those existing extensions (e.g., non-UK securities registered on a UK register or paired with UK shares) would be welcomed as this is not currently entirely clear from the consultation paper. In our view, these extensions could and should be removed altogether so that the territorial scope is limited solely to securities issued by UK incorporated bodies corporate.

What types of securities are within scope?

HMRC proposes to explore a simplified approach to defining the types of securities which would be within the scope of the STS.

- They intend to move away from the existing approach of defining scope broadly to include debt and equity securities generally and then carving out most debt securities (under the so-called 'loan capital exemption'). Instead, the approach will be to define the tax base as equity securities plus debt securities which have equity-like features (defined in similar terms to the loan capital exemption). In practice this should mean that the scope of the tax is similar to that of stamp duty.
- It will be specified that the grant of a security interest is outside the scope of the STS (which will remove a headache which often needs to be considered only to be dismissed under the current rules).
- The grant of call options and warrants would fall outside the scope of the STS but their transfer would be chargeable.
- Partnership interests would be taken out of scope subject to an anti-avoidance rule to prevent partnership interests being used as a method of enveloping share ownership in order to avoid the new single tax.

These proposals generally represent a welcome simplification of the existing regime.

Consideration

A core component of any tax is the amount or value on which it is to be charged, and here again the consultation proposes some welcome simplifications to the current position. At present, both stamp duty and SDRT are normally charged at 0.5% of the consideration for the relevant transfer (albeit, in the case of stamp duty, that the tax is then rounded up to the nearest £5). However, for stamp duty purposes only certain forms of consideration (cash, debt or other stock or marketable securities) are taken into account; SDRT on the other hand looks to any amount of money or money's worth that is given. This divergence will be removed under the proposed changes, with the STS adopting the SDRT 'money or money's worth' approach.

On the whole, this is a sensible suggestion which should remove some of the complexity and uncertainty around determining the appropriate consideration on which the tax is to be charged. (The current stamp duty treatment of debt as consideration, in particular, can give rise to some tricky points.) It is true that the STS will be payable in certain situations where no tax would currently be paid (typically where the consideration provided is in a form that does not attract stamp duty and an appropriate transfer instrument is executed to cancel any SDRT charge). However, the government is alive to this point and proposes specific exemptions for forms of consideration such as obligations to pay pension benefits or issuance of a life insurance policy where it wishes to avoid disrupting the industries concerned.

The other key element of proposed reform relates to consideration that is not (or cannot be) quantified. The existing rules in this area (particularly for stamp duty) are a complex patchwork of case law, statute and HMRC practice which differ according to the type of consideration and the reason it cannot be quantified. Moreover, the existing rules often require the consideration (and therefore the amount of tax) to be determined on the basis of certain assumptions with no 'reckoning up' if the amount of consideration subsequently turns out to be different from that assumed.

The STS will have a single set of statutory rules to deal with the various different types of unquantified consideration. These rules are based on the existing rules that deal with unquantified consideration for SDLT purposes, which most practitioners would agree is an improvement over the existing stamp duty position. In brief:

- Contingent consideration: Consideration that is contingent on some uncertain future event (e.g., deferred consideration in a fixed amount payable on condition of continuing employment of the recipient) is initially treated as if it will be paid in full and the return is made on that basis. This is the same as the current position. However, if and when the contingency occurs (or it becomes clear that it will not occur) the tax is recalculated and any 'excess' tax that was originally paid can be then reclaimed.
- Unascertainable consideration: Where the amount or value of the consideration depends on some uncertain future event (e.g., an earnout linked to profitability of a business over a future period), the consideration is initially calculated on the basis of a reasonable estimate (rather than on the maximum figure or some

other 'reference' figure as current stamp duty rules require). When the amount of the consideration ultimately becomes known the tax is recalculated and any 'excess' tax can be reclaimed (or any additional tax due paid).

- Ascertainable but unascertained consideration: Lastly, where the amount or value of the consideration does not depend on a future event but is nevertheless unascertained (e.g., based on the value of completion accounts of the target company which have not yet been finalised at the time the return is required to be made), the initial consideration is again calculated on the basis of a reasonable estimate with a recalculation and reckoning up when the final value is determined. This is effectively the same as the current position under HMRC's 'wait and see' approach but would have a clear statutory footing.

The ability to recalculate the amount of tax to ensure that the 'correct' amount is ultimately paid in all three scenarios will be particularly welcome.

Overlaid on the above, where the consideration is contingent or unascertainable and the future event on which it depends is more than six months away, it will be possible to apply for deferral; this means tax must be paid up front in respect of any ascertained (or ascertainable but unascertained) consideration but tax relating to the contingent or unascertainable element may be deferred for up to two years. By that time the value may be certain in which case tax can be paid on that amount. If it remains contingent or unascertainable at that date, then the rules above apply (although it may be that a more accurate estimation can be made than would have been possible when the initial return was made).

These changes should generally leave taxpayers in a better position than under the current regime. Those responding to the consultation may wish to provide input as to whether or not the two-year deferral period is long enough, e.g., by reference to earnout provisions they are seeing in the market.

Lastly on consideration, the consultation is silent on the existing rules that can in certain circumstances deem a market value consideration for transactions between connected parties. It is presumed that these will be retained but clarification on this would be welcome.

Exemptions and reliefs

The broad thrust of the proposals is to replicate the scope of existing reliefs. So, for example, the existing reliefs for intermediaries, stock lending, repurchase arrangements and securities admitted to trading on a recognised growth market are to be retained in their current forms.

The STS will also adopt the existing stamp duty relief for transfers between members of a corporate group. The current relief is subject to a number of complex and somewhat obscurely drafted anti-avoidance rules, so it is heartening to see that the government hopes to clarify and simplify the application of these rules in the new version of the relief (including dropping entirely a rule that denies relief where the securities in question were 'previously conveyed or transferred, directly or indirectly' by a non-group member).

Likewise, the STS will adopt the existing reconstruction and acquisition reliefs but HMRC intends to make the legislation clearer reflecting existing caselaw interpretations. It remains to be seen whether HMRC might, as part of that rewrite, reconsider its current policy (as expressed in STSM042415) that funded debt (for example, bonds) needs to be replicated at holding company level in order to secure acquisition relief under section 77 Finance Act 1986.

The most unwelcome news in this section of the consultation is that the existing £1,000 de minimis exemption from stamp duty will not be retained. This rule was originally introduced to simplify administration of the tax by taking a large number of low-value transactions out of scope. Under the STS the compliance burden of making a return will be much reduced (and will fall largely on the taxpayer rather than HMRC) which has apparently prompted HMRC to conclude that the rationale for having a de minimis exemption no longer holds good. The consultation paper does not address whether or not transfers for nil consideration would need to be reported.

Where next?

The scope of this consultation expressly does not include the 1.5% charge on the issuance or transfer of securities into a clearance system. The consultation paper notes that if modernisation is taken forward then the 1.5% charge will be dealt with separately. It will be interesting to see whether and to what extent the government proposes to take advantage of its post-Brexit freedom to tax such transactions, or whether it will instead repeal the 1.5% charge in order to maintain the status quo and attract investors to the UK market.

The consultation ends on 22 June 2023, and we would encourage practitioners to respond to it and any subsequent consultation on draft legislation to further bolster the case for reform, as well as to flag any potential areas which have scope to cause friction in practice.

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