

Confidential Filing

Sir E. Kaye's paper on  
Capital Taxation.

Economic Policy

October, 1979.

| Referred to                    | Date | Referred to | Date | Referred to | Date | Referred to | Date |
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MJ IABT

cc FS, HWT

10 DOWNING STREET  
LONDON SW1A 2AA

THE PRIME MINISTER

21 July 1989

*Dear Kenneth,*

Thank you for your letter of 17 July in which you referred to the question of 1982 valuations of unquoted shares for capital gains tax. I thought it might be best if I responded before we meet on Saturday.

This is a complicated issue which I know Nigel Lawson and Norman Lamont have looked at on many occasions over the last year or so. I understand that you yourself saw Norman Lamont to discuss it on 12 April.

You suggest in particular that there should be a one-year concession for married couples who did not understand that they could arrange to bring their pre-1982 holdings of unquoted shares together for valuation purposes. Having had one or two enquiries on the point, the Revenue thought it helpful to publish a Statement of Practice about it in May. But this was, I am advised, never an area where the words of the legislation left any room for argument. The Revenue's Statement set out the strict effect of the law. It may be that some taxpayers and their advisers did not fully appreciate the effect of the law: but if they were in doubt they could always have asked the Revenue, who would have told them the answer. I would see some difficulty in the Government agreeing to a concession which was introduced

*✓*

solely because some taxpayers might have arranged their affairs differently but for their failure to understand what the law meant. But I am sure that this is a question Norman Lamont will be able to cover when you see him again next week.

Yours  
Raymond

Sir Emmanuel Kaye, CBE.



PERSONAL

PRIME MINISTER

CORRESPONDENCE FROM SIR EMMANUEL KAYE

You will recall that earlier in the week Sir Emmanuel wrote to you putting you on warning that he would take the opportunity of your visit to Glyndeborne on Saturday to raise a tax matter.

I have had this looked into by the Treasury and Inland Revenue, and I now attach a reply to Sir Emmanuel for your signature. My advice is that:

- your reply should go to him before Saturday
- you should then decline to discuss the matter with him when you meet.

The main reason for this advice is that set out in paragraph 6 of the Inland Revenue brief which is also attached. You will see that it appears Sir Emmanuel would himself stand to gain from the retrospective special tax concession he proposes.

Content to sign and for us to transmit this tomorrow?

PP *Mananville*  
*Duty Clerk*

*Signed*  
*mt*

Paul Gray  
20 July 1989

P.S. I gather you may also be seeing Godfrey Bradman on Saturday; you might like to bear in mind his tendency to lobby on tax matters in which Rosehaugh has an interest.

MJLABS

PERSONAL



2017  
SR 2-NO.

Treasury Chambers, Parliament Street, SW1P 3AG

Paul Gray esq  
PS/Prime Minister  
No. 10 Downing Street

20 July 1989

*Dear Paul*

**CORRESPONDENCE WITH SIR EMMANUEL KAYE**

As requested in your letter of 18 July, I attach a draft letter for the Prime Minister to send to Sir Emmanuel Kaye. In case he still persists in raising the matter personally, I also attach a one-page brief.

*Yours,*

**S J FLANAGAN**



~~DRAFT~~ LETTER FROM THE PRIME MINISTER TO SIR EMMANUEL KAYE

*I think I thought it might be better if I responded before we met on Sunday.*

*Thank you for*

*17 July in Sunday*

In your letter of ~~27~~ you referred to the question of 1982 valuations of unquoted shares for capital gains tax. This is a complicated issue which I know Nigel Lawson and Norman Lamont have looked at on many occasions over the last year or so. I understand that you yourself saw Norman Lamont to discuss it on 12 April.

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10 DOWNING STREET  
LONDON SW1A 2AA

*From the Private Secretary*

18 July 1989

CORRESPONDENCE WITH SIR EMMANUEL KAYE

We spoke this morning about a letter the Prime Minister had received from Sir Emmanuel Kaye concerning the treatment of minority holdings in unquoted companies for inheritance tax and capital gains tax purposes. I now enclose the relevant extract from Sir Emmanuel's letter, and would be most grateful if you could arrange for the preparation of a draft reply for the Prime Minister to send him. If at all possible, it would be helpful to have this by close of play on Thursday 20 July. Apologies for the tight deadline.

PAUL GRAY

Steven Flanagan, Esq.  
Financial Secretary's Office  
HM Treasury

KK



# The Unquoted Companies' Group

Founded in 1968 to study the contribution made to the economy by the unquoted sector

Date: 17th July, 1989

The Rt. Hon. Mrs. Margaret Thatcher M.P.  
10 Downing Street  
LONDON SW1A 2AA

Please reply to:

Sir Emmanuel Kaye C.B.E.  
Hart House  
HARTLEY WINTNEY  
Hampshire  
RG27 8PE

Tel: (025 126) 3773

*My dear Prime Minister,*

Elizabeth and I are greatly looking forward to the pleasure of seeing you and Denis at Glyndebourne. As you know, I treat such events as purely social and relaxing occasions but on this visit I should much appreciate your advice on a Revenue/Treasury matter, particularly as you are First Lord of the Treasury! Therefore, I thought I should put you in the picture beforehand.

You will recall that the Chancellor's 1988 Budget abolished, for Capital Gains Tax purposes, pre-1982 inflationary gains and raised the rate of CGT from 30% to 40%. Accordingly, it became necessary to establish 1982 valuations for unquoted shares for CGT purposes.

Sir Anthony Jacobs, Chairman of the British School of Motoring, pointed out that there was an anomaly in the valuation of minority unquoted shares, which were subject to a heavy discount. In other words, a majority holder was given a proportionate valuation whilst the small shareholder was clobbered. I can best illustrate this by an example:

In the case of a company worth £200,000 in April, 1982, with two shareholders - one with 90% and one with 10% - the 90% stake would be valued at £180,000 but the 10% would be valued at £20,000 less a discount of 75%, or at only £5,000.

In his representations Sir Anthony had the support of some 200 major unquoted companies and he understands that some 90 MP's have written on this matter to Treasury Ministers. All suggestions made by Sir Anthony Jacobs and by The Unquoted Companies' Group to remedy this anomaly have so far been rejected.

There is a further, even more serious, anomaly. If, for instance, two of the shareholders in the £200,000 company were husband and

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wife, each with 30%, for Inheritance Tax purposes if one of them died the two holdings would be added together and valued as a majority holding. Thus, in my example, the two holdings would be 60%, or valued at £120,000 so that on the death of one Inheritance Tax would be payable on £80,000.

But if one of the spouses sold the 30% holding to a third party then, for CGT purposes, it would be valued as a minority holding subject to a discount of about 60%, or at only £24,000, and CGT would be levied on the difference between £24,000 and the sale proceeds.

The Revenue answer is that for Inheritance Tax purposes the holdings of spouses are added together to prevent avoidance by the splitting of holdings. Be that as it may, the effect remains that holdings of spouses are penalised by being valued at full value for Inheritance Tax and a very low value for Capital Gains Tax.

It appears that the Revenue recognise this contradiction by having had an unpublished practice of agreeing to treat spouses' holdings as one for the purposes of CGT if they employed the device of permitting one spouse to sell to the other one day before the sale to a third party (although this was not clear from the original legislation and seemed to invite "Furniss v. Dawson" treatment). In May this year the Revenue disclosed this practice by publishing a statement to this effect, on which publication they are to be commended.

However, all this is grossly unfair on those couples who were unaware of the unpublished practice and who sold their holdings to third parties between April 1988 and May 1989. Consequently, Sir Anthony Jacobs and I on behalf of The Unquoted Companies' Group, saw the Chairman of the Board of Inland Revenue, Sir Anthony Battishill, and explained that we are therefore seeking a Revenue concession that all such holdings of husband and wife since April, 1988 should be added together for CGT purposes. We gathered from Sir Anthony Battishill that such an Extra Statutory Concession by the Revenue was feasible provided the Treasury agreed. You will have noted that the Revenue publication establishes the practice of spouses selling to each other one day before a third party sale for all future years, whereas what we are seeking is a concession limited to one year only.

To obtain Ministerial agreement I wrote to Mr. Norman Lamont on 22nd June, 1989 (copy enclosed). Unfortunately, the two dates we had arranged to meet since then have both been postponed by the Treasury, although another is in the offing. I have always been received with courtesy and interest by Treasury Ministers and had hoped to have spoken to Mr. Lamont on this subject before now but that, of course, has not proved possible and I have so far not obtained any assurance that this one year concession to bridge the gap will be forthcoming.

With kindest regards,  
 Yours very sincerely  
 G. M. M. M. M.



# The Unquoted Companies' Group

Founded in 1968 to study the interests of the unquoted sector

Date: 22nd June, 1989

The Rt. Hon. Norman Lamont, MP  
Financial Secretary  
H. M. Treasury  
Parliament Street  
LONDON SW1P 3AG.

Please reply to:

Sir Emmanuel Kaye, CBE,  
Hart House,  
HARTLEY WINTNEY,  
Hampshire, RG27 8PE

*My dear Financial Secretary,*

I have come across a situation which bears upon our previous exchanges on the valuation of shares as at 1982 - but could also give rise to something which, if I may say so, you should take action upon.

The recently published Statement of Practice, no: SP5/89, which deals with the valuation of holdings at 31 March 1982, if they have subsequently been united, on the basis of the aggregate percentage they represent - e.g. a wife giving away a minority interest to her husband, to add to his minority interest, just before sale so that he sells a majority interest and his base value at 1982 is calculated as if it were the value of a majority holding - makes public something the Revenue have apparently been practising for some time. And yet my enquiries show that the Revenue practice was not known of, even in some of the major accounting firms, let alone among laymen.

This is very serious. It means that people who did know of the Revenue practice could organise themselves so as to obtain one base value calculation, while those who did not, and failed to do the very simple (almost artificial) thing of having a gift between spouses just before sale, could only get another. This is desperately unfair.

I suggest that the only way to correct this for people who did not know of the Revenue's unpublished practice is to add to the law - unless it can be done by Statement of Practice or by Extra Statutory Concession - a provision which is effective from 6th April 1988 (since the Revenue were operating that practice during the last tax year) and, at least for

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husbands and wives, operates to give them (whether one of them actually made a gift to the other or not) a greater valuation of their holdings as at April 1982 in the event of a subsequent disposal.

With kind regards & looking  
forward to your reply.

Yours sincerely,

Samuel.

## BRIEF

1. In 1988, capital gains tax was confined to gains since 1982: earlier gains were exempted. To measure post-82 gains, it is necessary to value assets at 1982.
2. For holders of shares, what matters is what the individual - shareholding was worth in 1982 - not the value of the company. When shareholders come to sell, their CGT is on the gains on their particular shares, not the increase in value of the company. Value is determined on what shares would have fetched in the open market in 1982. The approach used is the same as that for other tax purposes - inheritance tax, Schedule E benefits, etc.
3. A minority shareholding will be worth significantly less than a straight proportion of the value of the company. This is because the shareholder cannot control how the company is run.
4. Shareholdings in private companies have typically been split into minority holdings to give tax advantages - lower values for inheritance tax etc. The corollary is that these lower values will be reflected in the new 1982 CGT baseline. There have been a lot of representations that, one way or another, shareholders ought to be able to aggregate their holdings for 1982 valuations. The Financial Secretary has had many meetings with lobbyists. It would be very difficult to justify making a change of this kind without doing the same for valuations for other tax purposes - where the change would work heavily against taxpayers (leading to higher values and hence more tax) and be very unwelcome.
5. The law does allow husbands and wives to arrange for their shares to be aggregated for valuation purposes, by one spouse transferring his/her shares to the other before sale. This is the strict effect of the law: there is no room for argument or interpretation. But having had the odd enquiry, the Revenue thought it helpful to publicise the position in a Statement of Practice in May 1989. There is no question of the Revenue "concealing" an unpublished practice in an area where there is legal doubt: the position stems from the wording of the law.
6. Sir Emmanuel suggests there should be a special concession for married couples who did not appreciate what the law meant, and sold shares between April 1988 (when the new 1982 baseline came into being) and May 1989, and might have arranged their sale differently had they fully understood things. Other correspondence suggests Sir Emmanuel himself is in this position: he sold Lansing Bagnall recently, and it appears that shares were held by both him and his wife. Had he and his tax advisers asked the Revenue, they would have been told what the legal position was. It would be novel to make a concession for taxpayers who might have arranged things differently if they had fully understood the law or had better tax advice.



Prime Minister

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17.7.89

Sir Emmanuel Kaye rang me about  
the enclosed and delivered it today.  
As he is going to mention it on  
Saturday, shall I pass it to  
Paul Gray for comments for you  
before Saturday?

Gay

Yes - but we shall

find it difficult to get  
them by that time.



10 DOWNING STREET

THE PRIME MINISTER

10 October, 1979.

Dear Emmanuel,

Thank you for your letter of 3 October and for the copy of your submission to Geoffrey Howe on capital taxation.

As you probably know, Geoffrey has asked Arthur Cockfield to carry out a full review of Capital Gains Tax and Capital Transfer Tax; and I know he will be grateful for your great practical experience of these matters and the expertise with which the case is presented.

Yours ever,

(SGD) MT

Sir Emmanuel Kaye, C.B.E.



Prime Minister



Emmanuel Kaye  
has written to  
you three times  
in the last few  
weeks.

10 DOWNING STREET

PRIME MINISTER

Your request  
R 9/10  
S/L

Attached is a letter from  
Emmanuel Kaye together with a  
very detailed submission which  
he has sent to the Chancellor  
on capital taxation. I attach  
a draft letter which you might  
like to send in reply.

Let another letter?  
I signed with  
yes to Kaye?

Could  
you please  
sign.

5 October 1979

Mr  
S. G. 29  
R.

LANSING • BAGNALL • LTD



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RG21 2XJ

Sir Emmanuel Mayo, C.B.E.  
Chairman & Governing Director

Telephone Basingstoke (0256) 3131  
Telex 858120 Bagnall G Bsthe

The Rt. Hon. Mrs. Margaret Thatcher, M.P.  
Prime Minister  
10 Downing Street  
LONDON SW1.

3rd October, 1979

My dear Prime Minister,

CAPITAL TAXATION

When you were leading your spirited attack on capital transfer tax, you stated that you would repeal it and supported your statement with a number of weighty arguments but, nevertheless, some thought that this would not be feasible. However, you will be happy to know that you were fully in tune with a rising trend, since the Federal Governments of Canada and Australia have done just that.

Our work in preparing our representations to the Chancellor of the Exchequer on capital taxation has greatly strengthened our belief that there is a powerful case for the abolition, rather than the mere reduction or reform of capital transfer tax. Abolition is correct in principle, cheap in revenue terms, and strongly supported by the recent precedents I have quoted.

Abolition of the corresponding taxes in Canada and Australia has been widely welcomed, little criticised and has caused no political difficulties. Australia is particularly interesting because of its close cultural affinities with Britain and its strong trades unions, and its Labour Party. Australia has no capital gains tax either. This is the system we would like to see adopted in Britain.

The case for the abolition of capital transfer tax, as well as, alternatively, its mere reduction and reform, is set out in our representations and is briefly dealt with in our covering letter to the Chancellor of which I enclose a copy together with our submission. We have tried hard to make it the most comprehensive and thorough of those your Government is likely to receive on this subject - and we hope the most helpful.

With every good wish,  
Yours very sincerely,  
Emmanuel.







*Kingsclere Road  
Basingstoke  
Hampshire  
RG21 2XJ*

*Telephone Basingstoke (0256) 3131  
Telex 858120 Bagnallie Bthk*

*Sir Emmanuel Hays, C.B.E.  
Chairman & Governing Director*

3rd October, 1979

The Rt. Hon. Sir Geoffrey Howe, Q.C., M.P.,  
Chancellor of the Exchequer  
11 Downing Street  
LONDON S W.1.

*The Submission on Capital  
Taxation can be found  
in the attached folder.*

*My dear Chancellor,*

CAPITAL TAXATION

I have pleasure in submitting representations on Capital Taxation on behalf of the Unquoted Companies' Group, whose 21 members provide employment for 171,000 people and whose present insoluble capital taxation difficulties are echoed by thousands of other independent unquoted companies up and down the country.

We hope you will implement our proposals in the Budget and Finance Bill, 1980.

We have tried to make these representations the most comprehensive and thorough of those you are likely to receive on this subject. We have also done our best to make them helpful to you, especially by detailed costing of alternative reductions in the rate schedule and elsewhere, wherever possible. We suspect that our representations will contain numerous points of interest that will not be put to you by others; and we hope that it will be possible for you to give them your personal attention.

We ask you to consider very seriously abolishing capital transfer tax and capital gains tax. The combined yield of the remaining taxes on capital - stamp duty, development land tax and rates - would still be a larger proportion of gross domestic product than in any other European country, 4.13 per cent compared with an average of 1.66 per cent in our continental European partners.

At present, gifts of substance inter vivos often attract three taxes - capital gains tax, capital transfer tax, stamp duty. The abolition

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of capital transfer tax and capital gains tax would still leave stamp duty.

We recognise that abolition of capital transfer tax and capital gains tax goes beyond the policies to which the Government is committed. But the case for abolition is strong - in principle, in revenue terms, as a major simplification of the tax system and as part of the current trend in the English-speaking world (Canada and Australia), where abolition of taxes on capital has been widely welcomed and little criticised. Because the case for abolition has not received the attention it deserves, we explain it in our submission and urge that it be seriously considered as on balance much the most attractive option.

If, to our regret, you are not persuaded by the arguments for abolishing these two taxes, the submission lists a number of indispensable reforms, including tapering for capital gains tax and reducing the rate structure for capital transfer tax. It is partly because these reforms would account for a large part of the yield of these two taxes that we regard their abolition, rather than mere reduction, as the best and simplest solution.

When you have had an opportunity of considering the submission, the taxation committee of the Unquoted Companies' Group (4 members) would greatly appreciate being able to discuss it with you either in your office or, if you prefer to save your office time, over lunch or dinner.

Yours ever,  
Emmanuel.



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/over.....



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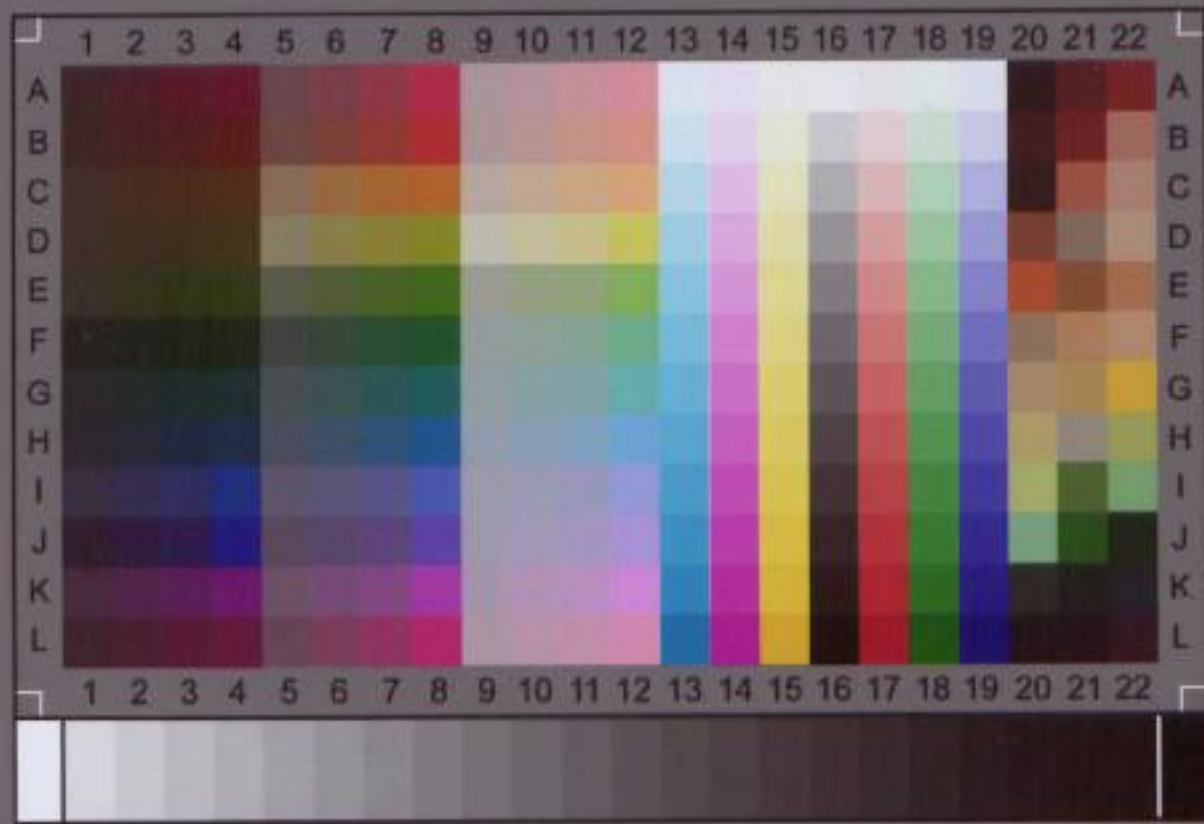
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Yours ever,  
Emmanuel.





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