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Capital Gains Tax & Entrepreneurs' Relief

For individuals, personal representatives and trustees, recent legislative changes introduced a new standard rate of capital gains tax (CGT), abolished both taper relief and indexation allowance for gains arising after 5 April 2008 and introduced entrepreneurs' relief for the disposal of certain business assets and qualifying shares.

Basic features – CGT

Individuals, personal representatives and trustees pay CGT at 18% on capital gains after deducting losses, entrepreneurs' relief and any annual exemption.

Companies pay corporation tax on any capital gains after deducting losses and indexation allowance.

The basic calculation

The gain or loss is broadly the amount by which the disposal value less any costs of disposal exceed the acquisition value plus any costs of acquisition.

The annual exemption

Gains of up to £10,100 for 2009/10 (2008/09 £9,600) are exempt from CGT for individuals and executors. The trustees' exemption is £5,050 for 2009/10 (2008/09 £4,800). If the same settlor has created more than one trust this annual exemption will be shared between the various trusts up to a maximum of 5.

Example

Gordon sells a painting in June 2009 for £20,000 bought in 1985 for £5,000. The gain is :

Sale proceeds	£20,000
Less : Original Cost	£5,000
Less: Annual exemption	£10,100
Taxable gain	£4,900
CGT @ 18% =	£882

Capital losses

Capital losses arising on the disposal of an asset are offset against gains in the same tax year. Excess losses are carried forward to relieve against future gains, but not so as to waste future annual exemptions.

Assets held at March 1982

If an asset was held at 31 March 1982 its value at that date is substituted for its cost in any CGT calculation.

Entrepreneurs' relief

From 6 April 2008 individuals and trustees disposing of qualifying business assets benefit from this relief which results in the first £1m of lifetime qualifying gains being taxed at an effective rate of 10%.

The following assets may qualify for relief provided they have been held for one year prior to the disposal:

- a sole trader's business.
- a share in a trading partnership.
- assets used in a sole trader's business which ceased within the preceding 3 years.
- shares in a trading company or the holding company of a trading group where the shares represent at least 5% of the share capital and carry 5% of the voting rights and the taxpayer is an officer or employee of the company.
- associated assets sold at the same time as the business/shares such as properties. (certain restrictions may apply to the amount of relief for these assets.)
- certain pre 6 April 2008 gains held over into EIS shares or Qualifying Corporate Bonds.

CGT – principal private residence

Gains on the sale of an individual's main or only home are exempt from CGT. This relief may be restricted where:

- the property stands in grounds exceeding half a hectare
- it has not been the only/main residence throughout ownership
- there has been some exclusive business use of part of the property

Spouses and civil partners may only hold one property per couple that qualifies for this relief.

Lettings relief may reduce any chargeable gain on a home which has been let as residential accommodation, subject to a maximum of £40,000, or the amount of the chargeable gain if lower.

Other exemptions/reliefs

- Gifts between spouses/civil partners do not attract CGT.
- Chattels – where the sale proceeds of most assets do not exceed £6,000, the gain is exempt.
- Most non business assets with a predictable life of 50 years or less are exempt from CGT.

Temporary non-residence

Disposals while temporarily living abroad may be chargeable to CGT upon return to the UK. If an individual was resident in the UK for any part of 4 years out of the 7 prior to leaving the UK and they return to the UK within a period of 5 years then gains made whilst abroad become taxable in the UK upon their return. Gains made in the year of departure are taxable in that year.

Non-domiciled persons

From 6 April 2008 UK resident non-domiciles (broadly those not born in the UK) will be taxed on their world wide capital gains unless:

- They have lived in the UK for more than 7 out of the last 9 years and opt to be taxed only on capital gains remitted to the UK. There is a £30,000 annual levy for taking this option which is payable in addition to the CGT on any remitted gains. They will also not be entitled to a CGT annual exemption.
- They have lived in the UK for less than 7 out of the previous 9 years and opt to be taxed on the remittance basis. There is no £30,000 charge for this but they will not be entitled to a CGT annual exemption.
- Total unremitted gains and income are less than £2,000 per annum. In which case the remittance basis can be used, no £30,000 levy is due and the annual exemption is available.

Deferral relief

It is possible to delay CGT due on a disposal by investing in the Enterprise Investment Scheme (EIS). EIS involves investment in new eligible shares in an unquoted trading company. The reinvestment must take place within a period 1 year before and 3 years after the sale of the original asset. Any gains deferred in this way effectively become payable upon a future sale of the shares in which funds were reinvested.

Gifts holdover relief

A gift or a disposal at a value less than market value can trigger a capital gain, especially where the transfer is between connected persons. On the disposal of certain assets it is possible to wholly or partly pass on the gain to the person who has received the gift. For CGT purposes this means that no capital gain accrues to the transferor, but the transferee is deemed to acquire it at either nil or a reduced value such that the gain deferred becomes payable by them upon a future disposal of the asset.

The relief is available upon the disposal of:

- assets used in the transferor's trade or his personal company
- shares in the transferor's personal company or an unquoted trading company
- certain agricultural property
- certain assets gifted to certain trusts

Bank/building society nationalisations

Shareholders in banks recently taken into public ownership/bought by another bank will be deemed to have disposed of their shareholdings for CGT purposes. If shares in one bank have simply been exchanged for shares in another then this does not constitute a capital disposal upon which CGT can be charged.

Executors

The estate of a deceased person benefits from a full annual exemption in the year of death and the two following years.

Summary

CGT is a complex tax with numerous exemptions, exceptions and rules. Careful consideration should be given to the disposal of any capital asset and appropriate advice sought, ideally in good time before the disposal.

What next?

This summary is intended to be illustrative only of the basic features of CGT. At BHP, we can advise upon all areas of CGT including business disposals, family CGT planning and investment disposals.

For a free consultation:

Contact your BHP Account Manager or one of our CGT specialists:

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