

# Capital Gains Tax Guide

Capital gains tax (CGT) has a nasty habit of landing investors with a hefty bill when least expected, so it pays to be prepared for any liability you may face.

## The basics

This tax is levied on money made from the sale of most assets other than your main home, so includes buy-to-let property - but some people are too busy celebrating their profits to consider its impact.

Yet it will contribute around £5 billion to government coffers in 2008 / 09 (Source: Budget 2008), so is not a tax to be sniffed at. This sum has been aided by soaring property prices over the past ten years which have outstripped any reliefs and allowances available to investors.

There are some exceptions to CGT and items such as cars and personal possessions up to £6,000 will not be liable. Gains on assets free of CGT include:

- Your main residence
- Government securities
- Qualifying corporate bonds
- National Savings certificates
- Individual Savings Accounts (ISAs)
- Life assurance policies
- Betting and lottery wins
- Compensation or damage awards

## How much?

Investors have an annual exemption (£9,600 in tax year 2008 / 09), but can easily slip over their limit when selling a big item, such as a second home or buy-to-let property, saddling them with a bill for tens of thousands of pounds or more.

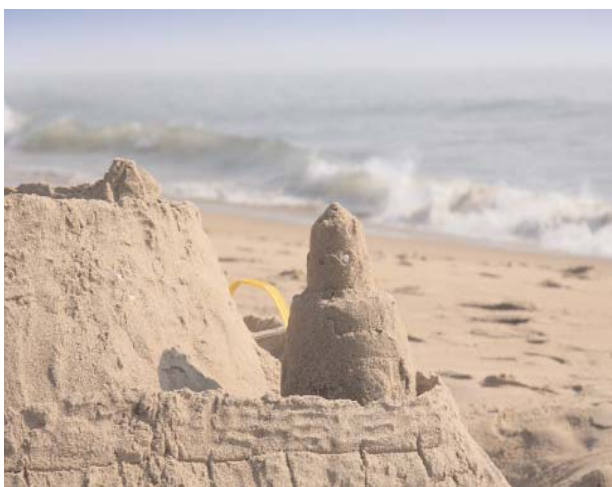
The CGT regime has been made much simpler as a result of tax reforms in Budget 2008. In place of a complex system of indexation and taper reliefs, capital gains above the annual exemption limit are taxed at a flat rate of 18%.

The only reduction to the 18% CGT rate is entrepreneurs' relief, which may be available in respect of gains made on the disposal of:

- All or part of a trading business the individual carries on alone or in partnership;

- Assets of the individual's or partnership's trading business following the cessation of the business;
- Shares in (and securities of) the individual's "personal" trading company (or holding company of a trading group);

- Assets owned by the individual and used by his / her "personal" trading company (or group) or trading partnership.



The first £1 million of gains that qualify for relief will be charged to CGT at an effective rate of 10%. Gains in excess of £1 million will be charged to CGT at the rate of 18%. Claims for entrepreneurs' relief on qualifying gains may be made on more than one occasion up to a 'lifetime' limit of £1 million.

Trustees will be able to claim relief on certain disposals of business assets and company shares and securities where a "qualifying beneficiary" has a qualifying interest in the business in question. Trustees must make claims jointly with the "qualifying beneficiary". Any relief given on the trustees' gains will reduce a beneficiary's £1 million lifetime limit on relief.

## Tax reform winners

As a result of the change to CGT, some recent buy-to-let investors could be big winners. If you bought a property solely as an investment two years ago and you have made a large gain on it, you'll now pay 18% on the whole gain. Had you sold the property in tax year 2007 / 08, a basic-rate taxpayer would pay at 20% up to the basic rate limit

and the balance at 40%, while a higher-rate taxpayer would pay 40% on the whole lot!

Even so, how can you lessen the burden of this tax, and maximise your profits on any assets which face CGT? Planning ahead to prepare for this tax can save you a tidy sum, and there are various ways to make the most of your tax-free allowances.

## Reducing the bill

One of the most simple and effective uses of the allowance is for married couples or civil partners to hold assets in joint names to double the allowance (assuming they own equal shares) that may be offset against the gain to £19,200 before CGT is payable. Provided you don't go over that limit, you won't have to pay any CGT, as long as you have not used up any of the allowance by disposing of other assets in the same period.

For property investment, the real saving comes if at some stage you have used it as your principal private residence (PPR). You don't normally face paying CGT on gains you make when selling your PPR - but you can also make use of it for other properties you own.

If you own an investment property, you can still make use of PPR relief by using it as your main home at some point before you sell it. This will give you the last three years' worth of growth free from CGT as well as the period in which you live there.

The Revenue does not specify how long you need to have lived there, but may ask for proof, and at least a six month stay is recommended.

If you let the property at some stage you will be entitled to up to £40,000 letting relief against your capital gain and this is available for each owner - so if it is in joint names, this doubles to a maximum £80,000. However, letting relief is only applicable to properties which have at some point been your main home.

Legal fees and stamp duty count as part of the cost of buying a property, as do selling costs such as estate agent fees - and these can be offset against any gains.

By the time you take off any available reliefs and the annual exemption, you may find that a large part of the capital gain has disappeared. This does not just apply to a second property, but it could also apply to a third or fourth property, both in the UK, or overseas.

Profits on shares and units trusts are liable to CGT, as are shares in investment trusts.

However, there is no CGT on shares or units held in an ISA or pension, for example, and there are special reliefs available for venture capital trusts or shares held for at least three years in an enterprise investment scheme. Business asset roll-over relief is also available, enabling the CGT payable on gains on a chargeable qualifying business asset to be deferred until a point in the future.

## Summary

CGT: Understanding the Basics

- A tax on the sale or gift of a chargeable asset.
- Annual exemption for each individual in 2008 / 09 is £9,600.
- An individual's assets on death are not liable to CGT.
- Some assets are exempt; for example, stocks and shares held in ISAs, National Savings Certificates, Premium Bonds, Child Trust Funds, cars, and personal possessions worth up to £6,000.
- Principal Private Residence (PPR) relief exempts gains arising on the sale of a property that has been the taxpayer's only or main residence.
- Tax is due on January 31st following the end of the tax year in which gain arose.
- It must be reported to HM Revenue & Customs if the gain exceeds annual exemption.
- Since April 2008, CGT is charged at a flat rate of 18% on gains above your personal allowance.
- Entrepreneur's relief on the disposal of certain business assets brings the CGT rate charged down to 10% on gains up to a lifetime limit of £1 million.
- Gifts between husband and wife or civil partners defer the CGT until subsequent disposal.
- Assets disposed of to a charity, museum or art gallery are free from CGT.
- A person must be resident or ordinarily resident in the UK, or be a temporary non-resident, for a CGT charge to arise.