

CAPITAL GAINS TAX – DO YOU NEED TO TAKE ACTION BEFORE 5 APRIL?

As you will no doubt be aware, from the extensive press coverage the Chancellor is making significant changes to the capital gains tax (CGT) regime from 6 April 2008.

Two major changes are the abolition of taper relief and indexation allowance for individuals, trustees and personal representatives.

These reliefs will be replaced with a single rate of capital gains tax of 18% and the recently announced Entrepreneurs Relief. Under these changes certain individuals and trustees disposing of certain types of qualifying businesses and shareholdings will effectively pay tax at a rate of 10% on qualifying gains of up to £1 million.

These changes mean that some taxpayers could stand to lose valuable reliefs if planning steps are not taken before 5 April 2008. Set out below is some basic information on each relief which will help you decide if you are affected by these changes.

Indexation Allowance

Although only available up to March 1998, in respect of assets acquired prior to this, the allowance is aimed at ensuring individuals are not taxed on inflationary rises in the value of assets. It may be of great value for people with assets that have reasonable base cost and which they have held for a considerable period of time. The maximum amount of indexation allowance that could be claimed is 104.7% of the Cost/March 1982 value of the asset.

As an example an asset with a March 1982 value of £50,000 would currently be eligible for £52,350 of indexation allowance thus increasing the base cost for capital gains tax to £102,350. The tax cost of losing this allowance is likely to be between £5,235 and £9,423 using post 5 April 2008 rules.

For assets with a significant base cost, calculations should be undertaken for all individuals, trustees and personal representatives to ascertain if significant indexation allowance is available and whether this can be crystallised without giving rise to a CGT charge.

Based on our current understanding there is scope for spouses/civil partners to lock in indexation allowance by undertaking a no gain no loss transfer between them. The manner in which the legislation works means that the spouse/civil partner receiving the asset will receive it with a base cost equivalent to the original cost plus any indexation allowance. Therefore, based on the rules issued by HMRC to date, following the transfer, the indexation is “locked in” to the base cost and will not be lost when the new rules come into effect on 6 April 2008.

Taper Relief

This relief was introduced in March 1998 and can reduce gains by up to 40% for non business assets and by up to 75% for qualifying business assets.

For disposals prior to 6 April 2008 qualifying for maximum taper relief can mean effective tax rates on chargeable gains ranging from 2.5% to 24%. In addition the definition of business asset for taper relief is likely to differ under the new rules for Entrepreneurs Relief. This means that there may be assets that under the Taper Relief regime qualified as a business asset which will not qualify for Entrepreneurs Relief under the new regime.

For assets with significant gains it is therefore important to review the position to ascertain if any action can be taken prior to 6 April 2008. In addition if you are considering disposing of an asset you should review the position to confirm whether the disposal should be deferred until after 5 April 2008.

Summary

If you feel that either of the above reliefs may significantly affect gains on assets that you hold then it is important that the position is reviewed. In the first instance please contact the partner in charge of your affairs to discuss your position. These matters are not straightforward and complications can arise with the use of March 1982 values and transfers between spouses. In addition there may be other issues which impact on the overall position e.g. VAT, Stamp Duty, Inheritance Tax, legal issues etc.

As previously stated, this is based on the recently published legislation as we understand it, although this could change prior to or after 5 April 2008. We cannot be responsible for any action you take or refrain from taking as a result of this information. No action should be taken without detailed professional advice.