

CAPITAL GAINS TAX OVERVIEW

Capital Gains Tax is a tax on the rise in value of an asset. CGT arises when an asset is "disposed of", which will usually be by a sale but will also occur on a gift or on the receipt of any capital sum where an asset is destroyed e.g. compensation or insurance proceeds.

Assets passing on death are not subject to CGT. Inheritance Tax may apply instead. Assets passing on death pass to the successors at the value as at date of death so that any latent capital gain is removed. On a subsequent disposal of the asset by a successor, he is deemed to have acquired it at the date of death value so that any "pre-death" rise in value is not taxed.

Individuals who are resident or ordinarily resident in the UK are subject to CGT on of their gains worldwide. Persons or companies who are neither resident nor ordinarily resident in the UK are not subject to UK Capital Gains Tax. This is in contrast with the position in many countries, including Ireland, where certain classes of assets such as land, mineral rights etc. are always subject to Irish CGT irrespective of the residence of the person disposing of them.

The definition of residence and ordinary residence is the same as for income tax. See our separate note on "Residence" and "Ordinary Residence" under UK tax law.

Certain types of assets are exempt from CGT with the result that neither the gains are taxable nor losses are allowable when they are "disposed of". Exempt assets include motor vehicles, principal private residence, gilt edge securities, qualifying corporate bonds, National Saving Certificates, foreign currency acquired for personal use, prizes, assets held in individual Savings Accounts and certain moveable goods.

A capital gain is calculated as follows. The sale proceeds or value is ascertained. Selling costs are deducted. Expenditure, including the original cost and the cost of

permanent improvements is deducted. In deducting acquisition costs and expenditure, only capital or improvement expenditure qualifies. Maintenance or repairs do not qualify. Acquisition costs such as stamp duty, legal fees and auctioneering fees are allowed. If the asset is given away, the person disposing of it will be subject to CGT based on the market value of the asset.

The capital gain is the difference between the sale monies received or disposal value, less the above deductions. In some cases, the market value is substituted for the actual proceeds. This applies to gifts or sales at under value. It is presumed that transfers between connected persons are at undervalue. Connected persons include family members and companies under the person's control or controlled by his family.

Indexation for inflation was allowed up to April 1998. As at that date certain generous allowances were introduced such as "taper" relief which could reduce the effect of rate of CGT down to 10% in many cases. In April 2008 a single 18% rate was introduced. By way of simplification many of the reliefs such as taper relief were abolished.

Prior to April 2008 taper relief applied depending on how long assets were owned. In the case of business assets the gain was reduced by 75% within three years so that the effective rate of tax was 10%. In the case of other assets taper relief kicked in more slowly so that 40% of the gain was reduced after 10 years.

There is a general annual allowance exemption for CGT of £9,600 for capital gains available to an individual in each year. If gains do not exceed this amount no capital gains tax is payable. If the annual exemption is not used in any particular year it is wasted. It cannot be carried forward.

A capital loss is computed in the same way as a capital gain. Capital losses on sales and disposals of assets in the current year are set off against capital gains in the same year. Capital losses can be carried forward against gains in future years.

CGT is due on 31st January following the relevant tax year. Payments on account are not required.

This Guide is intended as an overview and broad outline of the matters covered in it. Its purpose is to inform and raise awareness. We are happy to offer specific legal advice on particular circumstances.

This Guide should not be relied on as a substitute for comprehensive legal advice with reference to the particular circumstances.

While we have taken due care in the preparation of this publication, we do not accept legal liability as a result of any reliance placed on anything in this Guide. The reader should rely only on specific legal or taxation advice.

© Lavelle Coleman 2009