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BDO Stoy Hayward

BDO Stoy Hayward Northern Ireland
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Tax Newsletter

Pre-Budget Report

On Tuesday 9 October Alistair Darling presented his first Pre-Budget Report.

The following is an outline of a few of the issues which will have a significant impact on the majority of taxpayers.

Major capital gains tax reform

From 6 April 2008 the way in which Capital Gains Tax ('CGT') on the sale of a capital asset by individuals, trustees and personal representatives is calculated will be simplified.

From that date CGT will be calculated at a rate of 18% on the difference between the sale proceeds and the base cost of the asset, after deduction of the annual exemption (currently £9,200 for individuals and £4,600 for some trustees).

The 18% rate will apply irrespective as to whether the taxpayer pays income tax at the basic or higher rate.

There will no longer be any relief based on the length of ownership of an asset, specifically indexation relief up to March 1998 and taper relief from March 1998, and assets held at March 1982 will automatically be revalued at that date for the purposes of the calculation of CGT on disposal.

Other reliefs such as principal private residence relief, rollover relief for business assets, business asset gift hold-over relief and certain reliefs under the Enterprise Investment Scheme and Venture Capital Trusts will continue to be available.

This change is good news for higher rate taxpayers with non-business assets held for a short period of time, as they will see the tax rate charged on the disposal of such assets reduced from 40% to 18%.

However, for those with business assets held for two years or more the loss of business asset taper relief will mean that the effective rate of tax for higher rate taxpayers on the disposal of such assets is increased from 10% to 18%.

One area that will be greatly affected by this change is the disposal of a business, as is illustrated by the following example:

Paul is ready to retire and wishes to sell the shares in his family company.

The shares have a market value of £1,500,000 and he inherited them in March 1982 at a probate value of £250,000. They have no base cost.

If Paul sells the shares on 4 April 2008 he will pay CGT as follows:

	£
Disposal proceeds	1,500,000
Less cost	(250,000)
Less indexation allowance	(261,750)
	988,250
Less Business Asset Taper Relief at 75%	(741,188)
Chargeable Gain	247,062
Less Annual Exemption	(9,200)
Taxable Gain	237,862
Tax due at 40%	**95,145**

If Paul sells the shares on 7 April 2008 he will pay CGT as follows:

	£
Disposal proceeds	1,500,000
Less cost	(250,000)
Chargeable Gain	1,250,000
Less Annual Exemption (estimated based on current value)	(9,200)
Taxable Gain	1,240,800
Tax due at 18%	**223,344**

By delaying the sale by 3 days Paul has seen his CGT liability increase by £128,199.

As you can see, the reform of CGT will have a major impact on the disposal of business assets and we expect to see a lot of activity in this area between now and 5 April 2008.

On high value deals involving several million pounds the differential in tax on disposals before and after 6 April 2008 will be considerable.

Note: The calculation of corporation tax for companies in respect of their chargeable gains is unaffected.

If you are considering the disposal of a business asset it is imperative that you obtain professional advice on the impact of the new rules as soon as possible.

Residence and Domicile

As a direct result of the recent Gaines-Cooper case, from 6 April 2008 days of arrival in and departure from the UK will now be taken into account when determining whether someone is resident in the UK for tax purposes – previously such days where ignored.

Currently UK residents who are not domiciled in the UK and not ordinarily resident are only subject to UK tax on income or gains arising in or remitted to the UK.

From 6 April 2008 where a non-UK domiciled individual has been resident in the UK for seven years or more they will only be able to continue to use the remittance basis if they pay an additional tax charge of £30,000 a year.

Where an individual chooses not to use the remittance basis (and not to pay the additional charge) all their worldwide income and gains will be subject to UK tax, whether remitted to UK or not.

Previous years of residence will count from 6 April 2008, so if a non-UK domiciled individual has been resident in the UK for seven years or more on 6 April 2008 the new rules will apply to that individual immediately.

Anyone continuing to use the remittance basis for UK tax from 6 April 2008 will no longer qualify for UK personal allowances. If at a future point they decide not to use the remittance basis they will once again be entitled to UK personal allowances.

Current anomalies in the UK tax system which have been exploited by non-UK domiciled individuals to enable them to avoid UK tax on income and gains remitted to the UK are to be legislated against.

Inheritance tax for married couples and civil partnerships

Where a surviving spouse or civil partner dies on or after 9 October 2007, their estate will be allowed to utilise any unused nil-rate band of the first deceased spouse or civil partner when calculating the Inheritance Tax ('IHT') liability.

The date of the first death does not matter.

Elsie dies in November 2007 and leaves an estate with a value of £1,000,000.

When her husband John died in 1994 he left his whole estate to Elsie and so utilised none of his nil-rate band as no IHT is payable on transfers to spouses.

This means that Elsie's estate can utilise her nil-rate band of £300,000 plus 100% of John's nil-rate band (based on current values) of £300,000, i.e. £600,000. The amount exposed to IHT is therefore £400,000.

Before this change Elsie's estate would have had to pay IHT on £700,000, unless some planning using nil-rate band Will trusts had been in place.

To benefit from this change you must be married or in a civil partnership at the time of the first death.

If on the first death a proportion of the nil-rate band was utilised then it is the percentage remaining that can be utilised at the second death. For instance, if in the example above John had used up 10% of his nil-rate band by making a non-exempt transfer to his son, then Elsie's estate would have had 90% of his nil-rate band available, ie £270,000 – giving a total nil-rate band of £570,000.

If someone survives more than one spouse or civil partner the additional nil-rate band available to him or her will be limited to 100% of the nil-rate band applicable at his or her death, i.e. in the year ended 5 April 2008 the total nil-rate band available in respect of an estate is £600,000.

This change should make it simpler to protect the family home without the need for complex Will planning.

However, the changes do not remove the need for planning altogether, especially where an estate exceeds 200% of the nil-rate band (currently £600,000), or for those who are not married or in a civil partnership.

Other issues

Stamp Duty Land Tax ('SDLT')

A retrospective measure has been introduced to clarify legislation introduced in the Finance Act 2007 in respect of SDLT charged on transfers on an interest in a property within an investment partnership.

We shall advise further on the impact of this when the detailed legislation is published.

In addition, there is to be a consultation on the use of special purpose vehicles to reduce SDLT liability on high value residential property transactions.

Company Cars – Private Fuel Benefit

Employees who drive company cars and receive fuel for private use are charged tax on private fuel benefit calculated using a percentage based on the CO_2 emissions of their company car.

The fuel benefit multiplier will be increased from £14,400 to £16,900 on and after 6 April 2008.

If you are affected by any of the measures outlined above and require more advice please do not hesitate to contact us.

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