Broadcast

FACTSHEET: CAPITAL GAINS TAX

SPECIAL ISSUE

01753 888211
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SUMMARY OF THE OTS CAPITAL GAINS TAX REPORT

The Office of Tax Simplification (OTS) has published 'Simplifying by Design', the first report of its current Capital Gains Tax (CGT) review. It recommends some major changes to CGT including increasing tax rates and removing business asset reliefs. The report makes 11 recommendations in four main areas; rates and boundaries, annual exempt amount, business relief and interaction with inheritance tax. Here we examine these in more detail.

Rates & boundaries

Although many recommendations were made regarding rates and boundaries, the OTS noted two areas of particular concern. These were retained profits held by limited companies and share based remuneration for employees. The full list of recommendations made regarding rates and boundaries are as follows:

1 If the Government considers the simplification, priority is to reduce distortions to behaviour, it should either:

- Consider more closely aligning Capital Gains Tax rates with Income Tax rates; or
- Consider addressing boundary issues as between Capital Gains Tax and Income Tax

2 If the Government considers more closely aligning Capital Gains Tax and Income Tax rates it should also:

- Consider reintroducing a form of relief for inflationary gains
- Consider the interactions with the tax position of companies
- Consider allowing a more flexible use of capital losses

3 If there remains a disparity between Capital Gains Tax rates and Income Tax rates and the Government wishes to make tax liabilities easier to understand and predict, it should consider reducing the number of Capital Gains Tax rates and the extent to which liabilities depend on the level of a taxpayer's income.

4 If the Government considers addressing Capital Gains Tax and Income Tax boundary issues, it should:

- Consider whether employees and owner-managers' rewards from personal labour (as distinct from capital investment) are treated consistently and, in particular
- Consider taxing more of the share-based rewards arising from employment and of the accumulated retained earnings in smaller companies, at Income Tax rates

Annual Exempt Amount

This exemption is currently £12,300 and this is the level of net capital gains which can be made in a single tax year before Capital Gains Tax becomes payable.

The OTS suggests that the exemption could be reduced. Furthermore detail was provided on how to improve the current administration for reporting and paying Capital Gains Tax. The full list of recommendations made regarding the annual exempt amount are as followed:

5 If the Government's policy is that the Annual Exempt Amount is intended mainly to operate as an administrative de minimis, it should consider reducing its level.

6 If the Government does reduce the Annual Exempt Amount, it should do so in conjunction with:

- Considering reforming the current chattels exemption by introducing a broader exemption for personal effects, with only specific categories of assets being taxable
- Formalising the administrative arrangements for the real-time capital gains service and linking up these returns to the Personal Tax Account
- Exploring requiring investment managers and others to report Capital Gains Tax information to taxpayers and HMRC, to make tax compliance easier for individuals

Business Reliefs

In their report, the OTS reviewed the effectiveness of the current Business Asset Disposal Relief (previously known as Entrepreneurs' Relief) and Investors' Relief (IR). They specifically focussed on how to incentivise investment and providing relief for business owners on retirement and withdrawing from their business. The list of recommendations regarding business relief are as follows:

7 The Government should consider replacing Business Asset Disposal Relief with a relief more focused on retirement.

8 The Government should abolish Investors' Relief.

Interaction with Inheritance Tax/Capital Transfers

This section of the report is, arguably, the most complicated. As such we have summarised into three recommendations – all of which deal with Inheritance Tax in general. Recommendations are as follows:

9 Where a relief or exemption from Inheritance Tax applies, the Government should consider removing the capital gains uplift on death and instead provide that the recipient is treated as acquiring the assets at the historic base cost of the person who has died.

10 In addition, the Government should consider removing the capital gains uplift on death more widely, instead provide that the person inheriting the asset is treated as acquiring the assets at the historic base cost of the person who has died.

11 If the Government does remove the capital gains uplift on death more widely, it should:
- Consider a rebasing of all assets, perhaps to the year 2000
- Consider extending Gift Holdover Relief to a broader range of assets

In Summary

It is important to note that all of the above are, of course, just proposals and recommendations. Whether any are taken further or implemented in future remains to be seen. The full report can be viewed HERE.

A second report will be published next year which looks at 'key technical and administrative issues'.

For more information

Please contact a member of our team on **01753 888211** or email **info@nhllp.com**