Capital Gains Tax and Investments

Capital Gains Tax can reduce the gain on the disposal of your investments. The annual personal allowance for the tax year 2018-19 is £11,700. The annual allowance cannot be carried forward and any unused allowance is lost at the end of each tax year. Any gains above this limit are subject to Capital Gains Tax (CGT) rates. This guide explains methods of reducing your liability.

What is Capital Gains Tax?

Capital Gains Tax (CGT) is a tax on gains made on a UK resident's assets when they are sold or 'disposed of' e.g. when an asset is:

- sold
- given away
- transferred to someone else
- exchanged for something else.

CGT is charged on profits made on a one-off basis – e.g. - the sale of a holiday home.

How does Capital Gains Tax affect investments?

Income from stocks and shares are liable to Income Tax whilst profits made from the sale of those shares may be liable to CGT. Gains from certain investments are exempt from CGT and you can find more information on this later in this guide.

The disposals of shares, units in a unit trust and other similar investments are liable to CGT.

Gains on investments that are liable to CGT include:

- stocks and shares in a company
- units in a unit trust
- debentures, some bonds (excluding premium bonds) and certain securities.

You will pay CGT on gains made in excess of your annual Capital Gains allowance.

How much CGT will I pay?

Capital gains exceeding the annual exemption level of £11,700 are charged at either 10% or 20% (exception being gains on second properties which are taxed at 18% and 28%) depending on your other taxable income in the relevant tax year. Gains on disposals are added to your marginal rate of tax to determine the level of CGT payable. In this way part of your gain may be subject to basic rate CGT at 10% (or 18% for a second property) but gains when added to your taxable income which exceed the basic rate tax threshold will be taxed at the higher rate of 20% (or 28% for gains on a second property).

If you have potential gains that could be charged at the higher rate you should consider how to utilise your annual Capital Gains allowance. It is sensible to use the gain exemption against the potential higher rate to minimise the tax due.

Assets exempt from CGT

There are several assets from which gains are exempt from CGT, including your main residence. Chattels (moveable personal possessions) up to £3,000 are also exempt.

There are certain investments which are exempt from CGT, and these include:

- private investor gains from investment in gilts
- gains from stocks and shares you hold in tax-free investment savings accounts, such as ISAs
- gains on life insurance policies made by the original 'owner' of the policy
- gains on Venture Capital Trusts (VCT), as long as limits are met
- gains on an Enterprise Investment Scheme (EIS) provided they are held for three years
- gains on a Seed Enterprise Investment Scheme (SEIS), provided they are held for three years
- gains on qualifying corporate bonds.

Minimising CGT liability

There are certain strategies you may wish to adopt to keep your CGT liability to a minimum including:

1. Offset your losses against your gains

If you sell an investment and it makes a loss you can offset that loss against any gains you have made in the same tax year. If you have made greater losses than gains you can register those losses on your tax return and carry them forward to offset against gains in future tax years

2. Transfer to your spouse or civil partner

Each individual has their own Capital Gains allowance so you may wish to transfer some assets to your spouse or civil partner before selling them to make sure both allowances are fully utilised. This can be particularly useful if your spouse or civil partner pays tax at a lower rate than you. Transfers made to your spouse or civil partner are normally exempt from CGT.

3. Reduce your taxable income

The CGT rate is linked to the rate of Income Tax you pay, therefore, reducing your taxable income could minimise your CGT liability. One way to achieve this objective is to use tax shelters, such as ISAs. Income from an ISA is free from Income and Capital Gains Taxes. Other strategies include pension contributions, EIS or Gift Aid.

4. Sell when you pay tax at a lower rate

If you are aware that your Income Tax rate will reduce in the future you may choose to defer any sale of assets and wait until you are a basic rate tax payer which has the effect that you pay Capital Gains Tax at 10% as opposed to 20%, or 18% instead of 28% for gains on a second property.

If you would like to discuss any of the information provided in more detail, please contact your MPL adviser.

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