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To: Jack Clarke and Beth Roberts

From: Chartered Tax Advisers

Date: 8th November 2021

Subject: Advice on Property Transactions & General Tax Planning for Forthcoming Marriage

Introduction

This report considers the implications of the sale of The Old Rectory, the sale of 22 Westland Road and the purchase of a new main residence for Jack and Beth and potentially a replacement buy-to-let property.

It also considers any potential future income tax and inheritance tax planning that can be put in place to reduce tax paid.

This report has been prepared for and is address to Jack Clarke and Beth Robers and is intended for use by them only. No responsibility is accepted for any reliance placed on the contents of this report by third parties. It is based on tax legislation as it applies at the time of writing and any changes to the legislation may affect the conclusions of this report.

Contents

Section C - Mitigating Inheritance Tax

Abbreviations

The followings abbreviations are used in the report:

CGT - Capital Gains Tax
IHT - Inheritance Tax
PPR - Principal Private Residence
SDLT - Stamp Duty Land Tax

Executive Summary

The sale of The Old Rectory

- There will be no CGT liability arising for Jack as he has always lived in the property as his main residence and therefore receives PPR relief on the full gain.

- Jack will be liable to pay 50% of Rebecca's CGT arising on the sale, this will be £16,678 and must be paid within 30 days of completion of the sale.

- It is recommended that Jack tries to get Rebecca to agree to selling the property prior to his marriage with Beth. He can then use the proceeds he receives to purchase a new property for him Beth, as he will have no other property he will pay the basic rate of SDLT of £12,500 on the new property valued at around £450,000. This will be a saving of £9,750 if he jointly buys the property with Beth whilst she owns 22 Westland Road.

- Once Jack and Beth are married, Jack can transfer ownership of 50% of the property to Beth. If this is a gift then there is no CGT and no SDLT due.

22 Westland Road

- We recommend that you do not sell 22 Westland Road as it is providing additional income for you.

- Once you are married, we recommend that you transfer 70% of the property from Jack to Beth. As you will be spouses, this will be a no gain, no loss transfer for CGT. This means that if you sell the property in a different tax year to The Old Rectory then you can use both of your annual exempt amounts, plus the remainder of Jack’s basic rate band to minimise any CGT due, this could save about £4,563 in CGT. On the sale, there will be PPR relief available for whilst Beth lived in the property.

Income Tax

- It is recommended you make the above rental income election or Beth contributes £5,000 or more gross contribution to her personal pension in the tax year to reduce her adjusted net income below £50,000. This will mean that she does not suffer the high income child benefit charge of £547.

- We recommend you make a Form 17 election following the transfer of 70% of the ownership to Jack, so that you are taxed according to the beneficial ownership of the property. This will increase Jack’s income by £5,600 and reduce Beth’s accordingly, Beth will then not pay any tax at the higher rate. This election will save you £1000 per annum in income tax on the property income.

- The Marriage Allowance is not currently relevant to you as you both use your personal allowances.

Inheritance Tax

- Transfers between spouses once you are married are exempt from IHT. There is up to £1,000,000 of reliefs which will limit the amount of your joint estate charged to IHT once you both die.

- Transfers between each other prior to your marriage are potentially exempt transfers and may be chargeable to IHT if the transferring partner dies within 7 years of the transfer.

- There are several gifts you can make every year which will not be charged to IHT. Any regular payments you make which are deemed as made from your income, for example, to Oscar for living expenses, will be exempt from IHT.

Section A - The Sale of the Properties & Purchase of the New Property(ies)

Capital gains tax on the sale of any residential property is 18% for the basic rate, and 28% for any amounts exceeding the basic rate band.

Reliefs and taxes are based on selling the property in November 2021, these will change dependent on the date and amounts properties are sold for. Please let us know as soon as the property is sold as we will need to submit CGT forms within 30 days and pay any CGT due within 30 days.

Sale of The Old Rectory and purchase of a new joint property

If you choose to sell the Old Rectory then there will be a capital gain which arises from this sale, this will arise whether the sale is pre or post marriage. This is on the presumption that none of the ownership of The Old Rectory will be transferred from Jack to Beth after getting married.

Jack’s 50% share of the Old Rectory will have its capital gain reduced to zero due to as it will be covered by Private Principal Residence (PPR) relief and therefore no CGT will be due (Appendix 1).

As the sale will occur more than 9 months after Rebecca moved out, there will not be PPR available to cover the full gain that has arisen on her 50% ownership. Even though the property has remained your primary residence and Rebecca has not nominated another home as her own for PPR purposes, because it has not been transferred as part of your divorce she is not able to claim PPR relief for the period since March 2010 when she moved out. This will be deemed a period of absence for PPR purposes and any gain that has arisen in this period will be chargeable to CGT.

There will be PPR available to cover the last 9 months of the ownership, so the gain that arises in the last 9 months will receive relief too.

Under your seperation agreement, on the sale of The Old Rectory you will have to pay 50% of Rebecca’s capital gains tax bill that will arise. As shown in Appendix 1, if the property was sold this month then this will be £16,678. These figures will change slightly dependent on when the property is sold and the amount of proceeds received.

Further to the disclosure of Rebecca’s income and gains, part of her gain will be at 18% as she has £10,000 remaining of basic rate band and the remainder will be taxed at the higher rate of 28% CGT as it is disposal of a residential property.

This CGT will need to be disclosed on a capital gains tax on UK property online form within 30 days of selling the property, and this payment will also need to be made within the 30 days.

The money that Jack will have received following the sale and the payment of 50% of Rebecca's CGT will be £433,322.

If you are able to gain Rebecca's consent to sell The Old Rectory prior to your marriage, there may be a stamp duty benefit which arise on the purchase of a new property. If you are to purchase the new property in your own name initially, then as appendix 2 shows you will save £9,750 in stamp duty land tax (SDLT). This is because Beth still owns 22 Westland Road so this will be an additional residential property for her and therefore the higher rate of SDLT will apply to you both on the purchase.

Once you are married, you will be able to transfer 50% of the house to Beth. As you will be spouses this is done on a no gain, no loss basis so that there is not CGT due and Beth will inherit the base cost of the house at 50% of your purchase price.

If you choose to keep 22 Westland Road then you will keep your rental income from the property, we will discuss below how we can potentially structure this to minimise tax paid on this income.

Sale of 22 Westland Road and purchase of new home

If Beth decides to sell 22 Westland Road prior to their marriage then there will be a gain arising on the sale taxed on her. This is because she has not been using the property as her main residence for the whole time she has owned it. Beth will receive PPR relief from when she bought it until she moved in with Jack in December 2019 and then for the last 9 months of her ownership. The CGT which will arise on the sale of the property is shown in appendix 3, and will be £6,643.

There is no longer any reliefs that arise for the period in which the house was let to a third party as Beth would need to reside in the house to receive lettings relief, therefore gains that arise in the period from December 2019 until the last 9 months of ownership are chargeable to CGT.

If the sale of 22 Westland Road occurs after your marriage then Beth is able to transfer part of the property to Jack. This will allow the gain that arises to be potentially taxed at lower rates if it is sold in a different tax year to The Old Rectory.

If Beth transfers two thirds of the ownership of 22 Westland Road to Jack just prior to the sale, as it will be to her spouse this will be a no gain, no loss transaction. Jack will also inherit her property history and therefore receive PPR relief on the period in which it was Beth's main residence. When the property is sold, the gain that arises will be entirely covered by Beth's annual exempt amount, the gain that arises on Jack will be covered partially by his annual exempt amount and the remainder will be taxed at 18% due to him having available basic rate band (appendix 3). Due to Beth's income, her CGT will be 28% on a residential property. The transfer between spouses will be exempt from IHT.

Once Jack and Beth are married, they will also have to sell The Old Rectory under the terms of the seperation agreement. Therefore, they will also have the 50% CGT on Rebecca's gain as calculated in appendix 1. The cash they will have if both properties are sold after marriage and following any CGT due will be £881,191.

Neither Jack or Beth will then own a property, and any property purchased will suffer SDLT at the basic rate rather than the higher rate. The SDLT will be £12,500 on a property costing £450,000.

The remaining £50,000 would be invested into savings. It is possible to invest these funds into savings schemes whereby any interest arising will be exempt from income tax. You are individually allowed to invest £20,000 in an ISA and then any interest arising is tax free, therefore £40,000 of this can be invested in an ISA. You could also invest £50,000 in premium bonds, and any winnings that arise are exempt from income tax.

Replacement Buy-to-Let Property

The purchase of the buy to let property will be an investment property, and the capital purchase of this will not receive any tax reliefs. The SDLT arising on the purchase will be at the higher rate as it will be an additional property, on a £400,000 property the SDLT will be £18,250.

Recommendation

We recommend that if it can be negotiated with Rebecca, that you sell The Old Rectory prior to you two getting married. This is because it will allow Jack to get the proceeds from the property, and then there will not be the complexities in the joint ownership of the property going into the marriage. It will allow you to have a clean break from Rebecca.

We then recommend that Jack purchases the new joint property for the two of you prior to your marriage, this will mean that the SDLT due is paid at the basic rate as Jack will not own any other property.

On your marriage, Jack can transfer 50% of the property to Beth as his spouse on a no gain, no loss transaction. There will be no SDLT due on this transaction as there will be no consideration paid by Beth to Jack, if there is SDLT will arise. Please contact us if you wish Beth to pay Jack on the transfer as we will need to calculate any SDLT arising for you.

We recommend that for now you keep 22 Westland Road, this is because it is producing rental income for you. We will discuss below the best way to structure this income going forward. If you choose to sell it in the future, part of the gain arising on it will receive PPR relief as it was Beth's main residence for three years.

If you choose to sell 22 Westland Road, it would be beneficial for you to do so after your marriage in a different tax year to the sale of The Old Rectory. Beth can transfer part of the property to Jack, and this will allow the joint use of your annual exempt allowance and the remainder of Jack's basic rate band so that gains are taxed at 18% rather than 28%.

If you choose to purchase a further buy-to-let property, then the purchase will be a capital purchase and no reliefs will be received. The remainder of the profits which will be put into savings can be put into savings schemes whereby any income arising from them is exempt from income tax.

Section B - Mitigating Income Tax

It will be beneficial for Beth and Jack to equalise their incomes as this could reduce their potential exposure to the higher rate of income tax plus the high income child benefit charge.

Just so you are aware, there is an allowance called the marriage allowance which allows some married couples to transfer part of their unused personal allowance to their spouse. The marriage allowance will not benefit you are it is only beneficial to couples where one spouse does not use their whole personal allowance or has income falling with the 0% starting rate band. As both of you use your personal allowances, this is not currently relevant to you. It may be in future if one of you has a break from work for example for maternity or paternity reasons, but it would only be available if the other partner is not a higher rate taxpayer in that year.

The Married Couple's Allowance is only available where one spouse was born before 6 April 1935 so this will not be available to you.

High Income Child Benefit Charge

Even though Oscar is not Beth's child, as there are two partners in the household, there will be a high income child benefit charge on the partner with the higher income if it exceeds £50,000. This will be the case pre-marriage as Beth and Jack are living together, and also once they are married.

The high income child benefit charge claws back the child benefit that Jack received via Beth's annual self-assessment return. Appendix 5 shows the amount of child benefit clawed back from Beth every year.

Child benefit will be paid for Oscar to Jack until 31st August following his 16th birthday or if he continues in eduction or training that counts for child benefit (A Levels) until he reaches the age of 20. If Jack and Beth have a child before Oscar stops receiving child benefit, they will receve £13.95 a week for any more children until Oscar stop receiving it.

In order to avoid this charge, Beth can reduce her net income in a couple of ways which we will discuss below.

The first way would be to make gross personal pension contributions to reduce her adjusted net income. If she made gross contributions of £5,000 then her income would be £50,000 and subject to no charge. A £5,000 contribution will actually be a capital contribution of £4,000 from Beth and 20% tax relief at source. Beth can get further relief as this will also her extend her basic rate band of tax by £5,000. This will be beneficial in any year she makes capital gains as they will be taxed at 10% or 18% for a residential property for the amount of any basic rate band remaining.

The other way to reduce her income would be for Beth to transfer some or all of the rental profits from 22 Westland Road to Jack.

Rental Property

It is recommended that Beth diverts part of the rental profits she receives from 22 Westland Road to Jack once they are married.

Once you are married, income from a jointly owner property is automatically split on a 50:50 basis for income tax, irrespective of your actual beneficial interests.

Beth will need to make a transfer of 70% of the property once married. This will be a no gain, no loss transfer for capital gains tax and exempt from IHT. They must own the property as tenants in common and not joint tenants, if they own the property as joint tenants then the form 17 election discussed below will not be effective.

If they then make a Form 17 election this will allow them to split the income received from the rental on a 70% to Jack, 30% to Beth basis to reflect their actual ownership. This would mean that annually Jack would receive £5,600 of rental income and Beth would receive £2,400.

Beth's total income would then be £49,400. This would be below the high income child benefit charge and she would not suffer any clawback. None of Beth's income would be charged to tax at the higher rate band as her adjusted net income does not exceed £50,000.

Jack's increased income would be £36,600, this means that after deducting his personal allowance his income does not exceed the basic rate band. As Jack does not currently utilise his whole basic rate band (20%), altering the beneficial interest will shift some rental profits into this band and out of the charge to higher rate (40%) tax.

The tax saving of doing this transfer will be £1,000.

The election must be made, and Beth cannot just pay Jack the rental income as it will then stay full taxable on Beth.

If they sold the property, Jack and Beth would be charged to tax on their beneficial ownership of 70% and 30%. This could be modified just prior to sale as previously discussed to mitigate the capital gains tax as much as possible.

It is not recommended that a transfer from Beth to Jack occurs prior to their marriage, as this will be a transaction to a connected party and proceeds will be deemed to be market value. The gain arising on the transfer would be taxable even if it was gifted. Gift relief will not be available as it is not a business asset. There will also be IHT implications discussed below.

Oscar

If you wanted to, Jack could begin to invest in a Junior ISA for Oscar. Any income arising on this for Oscar will be tax exempt, even if Jack puts money into it up to a maximum of £9,000 per annum. Once Oscar turns 16 he can invest in a cash adult ISA and save up to £20,000. If you were to invest any money for Oscar's future this is the best way as if you provide funds for the benefit of a child in any other way, any income arising over £100 per annum will be taxable on the parent.

Section C - Mitigating Inheritance Tax

The Inheritance Tax threshold for married couples in 2021/22 is £650,000. This is when the first spouse passes away and leaves all of their assets to their surviving spouse, there is not IHT due on transfers between married couples. Therefore, when the deceased spouse dies their entire nil rate band of £325,000 will transfer to their surviving spouse and be added to their nil rate band of £325,000.

There is a further £350,000 of residence nil-band, which covers the main residence of the couple as long as it is closely inheritd by a lineal descendants. A lineal descendant includes children, grandchildren, great-grandchildren and a spouse of civil partner of such descendants. This is £175,000 per spouse, and again is inherited by the surviving spouse when the first spouse dies. This reduces the first £350,000 charged to IHT on the transfer of the main residence.

The amount of your properties will be included in your estate for IHT purposes, regardless of whether they are your main residence or let out on a long or short term basis.

This means that the first £1,000,000 of your estate will not be charged to IHT. Any transfer to each other once you are spouses in your lifetime or on your death is completely exempt from IHT. Based on your current value of assets of £900,000 (450,000 The Old Rectory + £450,000 Westland Road) there would be not IHT to pay.

You are also able to make the following transfers without opening up any liablity to IHT:

- Gifts to UK and EEA charities including political parties housing associations and national heritage bodies can be made of any amount and be free of IHT
- Small gifts of up to £250 to anyone in a tax year, if your gift exceeds this to any one person then the whole amount gifted to them in the year could be liable to IHT
- A gift from Jack to Oscar of up to £5,000 for his wedding gift, and if you have any more children they will also be able to receive this gift exempt from IHT. If you have grandchildren, you can make a gift of £2,500 on their wedding an be free of IHT, and you can make a gift of £1,000 on anyone elses wedding and be exempt from IHT.

You are able to give away £3,000 each year IHT free, and this will not be included as part of your estate.

If you make regular payments to anyone, for example, to Oscar once he starts his a levels or university for living costs then this will be habitual as neither Jack nor Beth will be left without sufficient income to maintain their normal standard of lviing. There would be no limit on the amount of money that can be transferred throughout your life in this manner.

It is not recommended that property is transferred between Jack and Beth before they are married. On the transfer, there would be no immediate charge to IHT as it is a potentially exempt transfer. However, there would be implications to IHT if it is gifted pre-marriage and the transferring spouse dies within 7 years.

This would mean IHT would arise on the transfer at 40% on the value transferred, this is likely to be nil assuming that this is the first gift that spouse has ever made. This is because the transferor would likely have two lots of annual exemption of £3,000 each (one from this year, and one from the previous year) and the nil rate band of £325,000 which would reduce the IHT charge.

There would be taper relief of a percentage dependent on the time period between the date of the gift and the date of death. This percentage reduces the tax payable, not the amount of the transfer.

Appendix 1

Sell The Old Rectory

Capital Gains Tax - Jack

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Proceeds = 900,000 x 1/2 =        450,000
Cost = (500,000 x 1/2) =         (250,000)
Gain =                            200,000
PPR Relief = 200,000 x 200/200 = (200,000)
Jack Gain =                            0
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PPR Relief - Jack

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|---------------------------|--------------|--------------|
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Period	Occupation	Non-Occupation
Mar 2005 - Mar 2010	60	
Mar 2010 - Dec 2019	117	
Dec 2019 - Nov 2021	23	
Total	200	

Capital Gains Tax - Rebecca

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Proceeds = 900,000 x 1/2 =        450,000
Cost = (500,000 x 1/2) =         (250,000)
Gain =                            200,000
PPR Relief = 200,000 x 74/200 =   (74,000)
Rebecca Gain =                    126,000
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CGT Due =
Gain =         126,000
Less AEA =     (12,300)
Taxable Gain = 113,700
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10,000 x 18% =   £1,800
112,700 x 28% = £31,556
Total =         £33,356
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Jack Share = 50% x £33,356 = £16,678

PPR Relief - Rebecca

Period	Occupation	Non-Occupation
Mar 2005 - Mar 2010	60	
Mar 2010 - Dec 2019		117
Dec 2019 - Nov 2021	14	9
Total	74	126

Basic Rate Band remaining = 37,500 - (40,000 - 12,500) = 10,000

Total Cash available to Jack after Sale =

Proceeds =	450,000
Less Rebecca 50% CGT =	(16,678)
Total =	433,322

Appendix 2

Stamp Duty on the purchase of new home in Jack's name

(125,000 x 0%) + (125,000 x 2%) + (200,000 x 5%) = 12,500

Stamp Duty on purchase of new home in joint names

(125,000 x 0%) + (125,000 x 5%) + (200,000 x 8%) = 22,250

Appendix 3

Sale of 22 Westland Road pre-marriage

Capital Gains Tax - Beth

Proceeds =	450,000
Less Cost =	(300,000)
Gain =	150,000
Less PPR relief = 150,000 x 44/58 =	(113,793)
Taxable Gain =	36,207

PPR Relief - Beth (assuming sale in November 2021)

|---------------------------|--------------|--------------|

Period	Occupation	Non-Occupation
Jan 2016 - Dec 2019	35	
Dec 2019 - Mar 2021		14
Mar 2021 - Nov 2021	9	
x		
Total	44	58

CGT Due =

Gain =	36,207
Less AEA =	(12,300)
Taxable Gain =	23,907

23,907 x 28% = £6,694

Total = £6,694

Total Cash available after Sale =

Proceeds =	450,000
Less Beth CGT =	(6,694)
Total =	443,306

Sale of 22 Westland Road post-marriage, transfers meaning Jack owns 1/3 of the property just prior to sale

Capital Gains Tax - Beth

Proceeds = 450,000 x 1/3 =	150,000
Less Cost = 300,000 x 1/3 =	(100,000)
Gain =	50,000
Less PPR relief = 50,000 x 44/58 =	(37,931)
Taxable Gain =	12,069

CGT Due =

Gain =	12,069
Less AEA =	(12,300)

Taxable Gain = 0

Capital Gains Tax - Jack

Proceeds = 450,000 x 2/3 =	300,000
Less Cost = 300,000 x 2/3 =	(200,000)
Gain =	100,000
Less PPR relief = 100,000 x 44/58 =	(75,862)
Taxable Gain =	24,138

CGT Due =

Gain =	24,138
Less AEA =	(12,300)

Taxable Gain = 11,838

11,838 x 18% = 2,131

Total Cash available after Sale =

Proceeds =	450,000
Less Beth CGT	= (2,131)

Total = 447,869

Appendix 4

Option	Proceeds	CGT	Cash in Bank
Sell TOR before marriage	450,000	16,678	433,322
Sell TOR after marriage	450,000	16,678	433,322
Sell 22 WR before marriage	450,000	6,694	433,306
Sell 22 WR after marriage	450,000	2,131	447,869

Appendix 5

High Income Child Benefit Charge

Beth adjusted net income

Trading Profits 47,000
Rental Profits 8,000
55,000
Less Threshold (50,000)
5,000

Charge = 5000/100 x 1% = 50%

Claimed 21.05 x 52 = £1095
50% = (£547)

£548