Chartered Institute of Taxation
Excellence in Taxation

The Chartered Tax Adviser Examination

November 2019

Taxation of Individuals

Suggested solutions

ANSWER 1

Our address

Your address

6 November 2019

Dear Ms Applegate

I have set out below our advice on your UK residence status for 2018/19 and an analysis of your Capital Gains Tax (CGT) position.

Statutory residence test

Since April 2013, the UK has had a Statutory Residence Test ("SRT") which determines whether an individual is resident in the UK.

The SRT has three parts:

1) Automatic overseas tests.
   If any of these tests are met, you are automatically not UK resident.

2) Automatic UK residence tests
   If any of these tests are met, you are automatically UK resident

3) 'Sufficient ties' test
   This evaluates personal UK connections and days spent in the UK. It is only considered if none of the above tests are met.

2018/19 UK residence

First, the automatic overseas tests are considered. There are three tests and during 2018/19 you did not meet any of these.

Second, the automatic UK residence tests are considered. There are three tests as follows:

Test 1
You were present in the UK for more than 183 days

Test 2
You had a "home" in the UK

Test 3
You worked full-time in the UK for the whole year.

You currently do not meet tests 1 or 3.

The meaning of "home" is complex but as you lived in your flat in Birmingham from 15th December 2018 onwards and this is your only home, you meet the second automatic UK test and will be UK resident.

Split year treatment

The SRT determines your residence status for an entire tax year, however when an individual starts to live in the UK, the year can possibly be split into a UK and a non-UK part. For split year treatment to apply, you must meet the conditions for one of the relevant cases. There are four cases relevant to your circumstances:

1) You started to have your only home in the UK
2) You started working full time in the UK

3) You ceased working full time abroad
4) You started to have a home in the UK

Provided you remain UK resident and retain your UK home throughout the 2019/20 tax year, you meet the conditions for all cases and split year treatment will apply.

The exact date your UK residence began will be a different date for each case.

The case which takes priority in these circumstance is 3) in the list Therefore the last day of your non-UK residence was 10 December 2018, when you stopped working for Westgate.

This means that 2018/19 is split into two parts. The UK part began on 11 December 2018. Split year treatment applies automatically and does not need to be claimed.

CGT analysis

You are not subject to CGT on gains realised when non-resident. Anti-avoidance legislation brings into charge any gains realised during periods of short term non-residence if you meet the following conditions:

- you were UK resident for 4 out of the 7 years prior to leaving the UK and
- you are non-resident for fewer than 5 years.

You meet both the conditions and are therefore subject to UK CGT in the year of your return on any chargeable gains realised whilst you were non-resident.

Chargeable gains:

	£
Shares (W1)	16,300
Investment property (W2)	15,000
	31,300
Less: EIS reinvestment relief (W3)	(15,000)
Less: AE	(11,700)
Chargeable gains	4600
CGT liability (W4)	£920

You should report the chargeable gains on your 2018/19 tax return. The tax is due by 31 January 2020.

You have not provided any details of transactions carried out between 2015/16 and 2017/18. If you require advice for this period, please let me know.

Yours faithfully

Mr T Manager

(W1) Shares

		£
Proceeds*	4.50* x 12,250	55,125
Cost**		(38,825)
<u>Gain</u>		**<u>16,300</u>**

* You are connected to your son for the purposes of CGT. Where an asset is disposed of to a connected person, the consideration used is the market value.

** Pool

Date	Price (£)	#	Cost (£)
01/01/13	2.45	5,000	12,250
04/03/14	3.50	1,250	4,375
16/03/14	3.70	6,000	22,200
		<u>12,250</u>	**<u>38,825</u>**

(W2) Flat

	£
Proceeds	465,000
Cost	(450,000)
<u>Gain</u>	**<u>15,000</u>**

(W3)

EIS reinvestment relief can be claimed when proceeds from any asset are reinvested in EIS shares. To claim the relief, you must be UK resident at the time of the gain and the reinvestment.

£15,000 of capital gains are deferred until there is a future chargeable event. There will be a chargeable event if you sell your EIS shares, you cease to be UK resident within 3 years from the date of the issue of the shares or the shares cease to qualify as EIS shares.

(W4)

The rate of CGT will depend on Janine's other income. It is presumed that Janine is higher rate taxpayer for the purpose of the calculation.

Janine can choose which gain to defer using EIS reinvestment relief and it is beneficial to defer the investment property gain as this attracts a higher rate of CGT.

MARKING GUIDE

TOPIC	**MARKS**
2018/19 residence status	
No overseas test met	1
"home" test met	1
Split year treatment	
Treatment available	1
4 cases to consider and all cases are met	1
Case 3 takes priority/Correct split year date	1
Split year applies automatically	½
CGT analysis	
Temporary non-residence rules	1
Chargeable in year of return	½
Should consider any other gains realised whilst non-resident	1
Greatstone plc shares	
Connected persons	1
Correct gain	1½
Gain on London flat	½
EIS shares	
EIS reinvestment relief available	1
Gain deferred until future chargeable event	1
Gains should be reported on tax return and deadline for payment	1
Presentation and higher skills	1
TOTAL	**15**

ANSWER 2

<u>Notes for meeting with Becky Clark</u>:

The shares Becky will receive in Green Ltd will be Readily Convertible Assets (RCAs). Shares are treated as RCAs if the issuing company is not entitled to a Corporation Tax deduction in respect of the shares awarded.

A Corporation Tax deduction is available if the shares awarded are in either:

(a) a company that is not under the control of another company, or

(b) a listed company (or the subsidiary of a listed company)

As Green Ltd is under the control of a company that is not a listed company (Yellow Ltd) no Corporation Tax deduction is available for Green Ltd and the shares will be classed as RCAs.

As the shares are RCAs they will be subject to Income Tax and National Insurance via payroll.

Assuming Becky has no income except from her income from Green Ltd she will pay tax at 40% on the market value of the shares at the date they are gifted to her.

In this instance there is no restriction on amount of tax that can be withheld under PAYE, meaning that the tax payable will exceed her cash salary payment for the month in which the gift is made.

Becky will need to reimburse Green Ltd for the tax paid no later than 90 days after the end of tax year in which the shares are transferred to her. If she does not then the amount not reimbursed will itself become liable to Income Tax and Class 1 National Insurance.

Alternatively Green Ltd may offer to loan Becky the necessary funds to pay the tax due on the gift. If this was the only loan that is made to Becky during the tax year then no benefit in kind would arise, even if the loan was interest free, because it does not exceed £10,000. (Becky's tax bill will be £8,000).

Becky will also be liable for Class 1 National insurance on the market value of the shares. Due to her salary level this will all be at 2%.

In contrast to the rules for paying over the Income Tax due on the gift, where there are insufficient cash funds for an employee to be able to meet their National Insurance liability in full in the pay period in which the gift is made, the balance can be collected from subsequent cash payments in the same or subsequent tax year.

When Becky eventually disposes of her shares in Green Ltd this may give rise to a Capital Gain. The base cost of the shares is deemed to be the market value of the shares at the date she received them.

Becky might wish to ask Rachel if she could be given some shares in Yellow Ltd instead of the 10 shares in Green Ltd.

As Yellow Ltd is not under the control of any other company the shares would not be RCAs, meaning that the tax due would be payable via the self-assessment system rather than through PAYE and no National Insurance liability would arise.

<u>Notes for meeting with Patrick Smythe:</u>

The conversion of the shares is a chargeable event and will give rise to a post-acquisition tax charge under s.438 ITEPA 2003.

The taxable amount is the difference between the value of the securities before and after the conversion took place. A deduction can be made for the consideration made by Patrick for the conversion of the securities. Therefore Patrick will have additional employment income of £3,500 (W1) for 2019/20.

On the sale of the shares a Capital Gain of £4,000 will arise (W2). If Patrick makes no other gains in 2019/20 this amount will be covered in full by his annual exemption. Otherwise it will be taxed at 10% / 20% depending on the level of his income.

If you require any further information please let me know.

Tax Manager

Patrick Smythe - Workings

Working One

	£
Market value of shares after conversion	12,000
Market value of shares immediately before conversion	(7,500)
Amount paid by Patrick	(1,000)
Employment income	3,500

Working Two

	£
Proceeds	13,500
Less:	
Amount paid by Patrick	(1,000)
Amounts charged to Income Tax (£5,000 + £3,500)	(8,500)
Net gain	4,000

MARKING GUIDE

TOPIC	**MARKS**
Shares in Green Ltd are RCAs	2
Tax and National Insurance via the payroll	½
Tax and National Insurance charged on market value at date of gift	½
Tax at 40%	½
No restriction on amount of tax that can be withheld	1
Reimburse Green Ltd for tax within 90 days to avoid further tax and National Insurance	1
Green Ltd could make a loan to Becky, no tax implications as less than £10,000	1
National Insurance at 2%	½
Mechanism for repaying National Insurance that exceeds available cash	1
Sale of shares will give rise to potential Capital Gain	½
Base cost of shares for Capital Gains Tax purposes	½
Suggest Becky receives shares in Yellow Ltd instead	1
Conversion is a chargeable event	1
Based on difference between market values before & after conversion	1
Deduction for amount paid by Patrick	1
Calculation of capital gain	1
Note re use of annual exemption / 10% or 20% CGT	1
TOTAL	**15**

ANSWER 3

1) Adam's taxable income and gains for 2019/20

On grant of original lease, the premium will have been split as follows:

Premium in the hands of Robin Ltd

	£	£
Premium		100,000
Capital element	2% x (100,000 x (30-1))	(58,000)

Property income for Robin Ltd		£42,000
		======

On grant of sub-lease

	£	£
Premium		20,000
Capital element	2% x (20,000 x (10-1))	(3,600)

		16,400
Deduction for original premium paid	42,000 x 10/30	(14,000)

Property income chargeable to Adam		2,400
Rent receivable from Starling Limited		2,500
Rent payable under the head lease		(1,500)

Total taxable property income for 2019/20		**£3,400**
		=====

Capital gain on the grant of the sub-lease

	£	£
Premium		20,000
Allowable cost (note 1)	£86,000 x (72.770-46.695)/87.330 x 20,000/50,000	(10,032)
Charged as property income	As above	(2,400)

Chargeable gain		**£7,568**
		=====

Note 1

Actual premium received	£20,000
Notional premium to give same rent as on head lease	£50,000

	Years	Lease %
Lease percentages		
On grant of head lease	30	87.330%
On grant of sub-lease – years remaining on head lease	20	72.770%
At end of sub lease – years remaining on head lease	10	46.695%

Cost of lease reduced by amount claimed by Adam

Cost of lease	100,000
Income tax relief claimed £42,000 x 10/30	(14,000)

	86,000
	=====

2)

Option a

If Adam buys the property outright, he will be able to claim a deduction for the interest paid on the loan.

Generally there will be no deduction for the cost of the property against trading income.

On sale of the property, he will be liable to Capital Gains Tax on the increase in value of the property and will be able to deduct the original cost of the property in the calculation.

If Adam purchases the new building, he could roll the gain on the grant of the sub lease over against the cost of the new building. However, as the gain will be covered by his annual exemption, this would not be advisable.

Option b

The lease premium will be split between the capital element and the income element as follows:

	£	£
Premium		80,000
Capital element	2% x (80,000 x (10-1))	(14,400)

Property income for lessor		65,600
		======

Adam will be able to make the following deductions in his accounts each year:

	£
1/10 of the property income element of the lease premium	6,560
Rents paid under the lease	10,000
Interest on loan to purchase lease	2,000

Total annual deduction	18,560
	=====

Adam will not get any tax relief on the capital element of the premium of £14,400 assuming he does not assign the lease before the end of the term, as this is a wasting asset.

Option c

If Adam rents the property for £20,000 per annum, he will be able to claim a deduction for the full amount of rent paid each year.

Comparison of total costs

	Option a - £	Option b - £	Option c - £
Initial lease premium	0	80,000	0
Rent payable over 10 years	0	100,000	200,000
Interest payable on loan	200,000	24,000	0
	-----------	----------	-----------
Total outgoings	200,000	204,000	200,000
	======	======	======
On which tax relief can be claimed	200,000	185,600	200,000
	======	======	======

Conclusion

If Adam purchases the property outright, although the annual interest cost will be the same as the annual rent if he rented it, he will own the asset at the end of the period which he would then be able to sell on if he no longer needs it. Alternatively, he could also continue to use the property indefinitely without having to renegotiate the lease after 10 years.

However, he should consider whether the property could go up or down in value over the period of ownership as this should also be factored into the decision as the loan will need to be repaid. In addition, if interest rates were to rise then this would affect the amount of interest payable.

Of the two leasing options, option c is more attractive than option b as the overall cost is less and the amount on which tax relief can be claimed is greater. Although the rent is higher, no loan is required and the whole amount paid is tax deductible.

Adam needs to consider whether property prices are likely to increase over the next ten years, with interest rates remaining low, in which case option a would be the better choice, or whether the future of the property market and interest rates look too uncertain, in which case option c would be better.

MARKING GUIDE

TOPIC	**MARKS**
Calculate property income element of original lease premium	1
Calculate capital element of sub-lease	1
Deduction of original premium in income calculation	1
Deduct rents payable under head lease	1
Correct total rents taxable for 2019/20	1
Correct restriction using lease %	1
Restrict allowable cost actual premium/notional premium	1
Restrict original cost for income tax relief claimed by Adam	1
Correct chargeable gain	1
Rollover relief could be claimed but not advisable	½
Interest on loan would be deductible under options a and b	1
Capital gain/loss when a is sold	½
split lease premium on b income:capital	1
Can claim 1/10 of income element of lease premium under option b	½
B is a wasting asset – no relief for capital unless assign during lease	½
Rent is deductible in B and C	1
Conclusion	1

TOTAL	**15**
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ANSWER 4

Mr D Stevenson
1 Town Avenue
PA1 EFG

City Tax Advisers
High Street
PA1 ABC

November 2019

Dear Daniel

Thank you for your letter.

Your Employment

Employees who are not directors are taxed on their earnings at the date of receipt. The date of receipt is the earlier of the date the individual becomes legally entitled to the earnings and the date they are actually paid. Therefore as you became entitled to your final wages payment from Harry's Kitchens on 25 March 2019 this income will be taxed at that date.

The payment of your conveyancing fees by Blissful Bathrooms will not give rise to a tax charge. Qualifying relocation expenses of up to £8,000 are exempt and the fees for both selling your old home and purchasing your new one fall within the definition of qualifying relocation expenses.

I note that you receive a fuel allowance, which is paid to you through Blissful Bathrooms' payroll. You will be able to reduce your overall tax liability by making a claim for tax relief on your qualifying mileage.

You cannot claim tax relief on any private journeys that you make, or on any "ordinary commuting," but you can claim for journeys that you are obliged to make in the performance of your employment and on travel to a temporary workplace.

Ordinary commuting is travel from your home to your permanent workplace. A permanent workplace is one where an employee must have spent, or be expected to spend, more than 40% of their working time over a period lasting more than 24 months.

It is possible for an employee to have a geographical area as their permanent workplace if the following conditions are met:

1) The employee has no other permanent workplace
2) The employee attends the area in the performance of their duties
3) The duties of the employee's job are defined by reference to a geographical area

You attend various Blissful Bathrooms outlets in Wales to perform the duties of your employment with no set working pattern. Therefore, the geographical area of Wales will be your permanent workplace. Travel from your home to the edge of this area is ordinary commuting. However, you can claim tax relief on your journeys within the area.

A temporary workplace is one that an employee attends to perform a task of limited duration, or for some other temporary purpose, for a period of less than 24 months.

As you did not work at Blissful Bathrooms' head office in Liverpool for more than 24 months (and there was never any intention for you to do so) this will be classed as a temporary workplace, meaning that you can claim tax relief for the mileage incurred.

The amount of the claim would be the number of qualifying miles that you have travelled in the year at the following rates:

45p per mile for the first 10,000 miles per annum
25p per mile thereafter

If this amounts to less than £2,500 you can make a claim using form P87 or through your personal tax account online and you must make the claim no later than fours year after the end of the tax year to which it relates.

If the claim is for more than £2,500 it must be made via the self-assessment system.

Unfortunately you will still suffer a National Insurance charge on the fuel allowance.

You may wish to consider asking Blissful Bathrooms if they would be willing to pay you mileage at the rates stated above in place of the fuel allowance as this would be more tax efficient.

If you do receive a gift from Blissful Bathrooms at Christmas then this will be covered by the trivial benefits exemption as long as it does not state within your employment contract that you will receive it, the cost does not exceed £50 and it is not given as a reward for service. If these conditions are not met then a taxable benefit in kind will arise based on the cost of the gift. This benefit will be shown on a P11D form, which your employer should provide to you by no later than 6 July following the end of the tax year. You would not be liable to pay any National Insurance on the benefit.

Holly's Pension

There is a limit in place on the total value of pension benefits that an individual can benefit from during their lifetime without triggering a tax charge. This limit is known as the Lifetime Allowance. For the year ended 5 April 2019 the Lifetime Allowance was £1,030,000 and if it remains at a similar level a tax charge will be triggered when Holly starts to draw her second pension.

Holly used 70% of her Lifetime Allowance in 2013/14, meaning that she will be entitled to 30% of the Lifetime Allowance in force when she starts to draw her second pension.

Holly's pension fund will be split between an authorised fund (covered by her remaining Lifetime Allowance) and a non-authorised fund.

The amount of the authorised fund will be equal to the unused balance of Holly's Lifetime Allowance and the first 25% of this slice of the fund can be drawn tax-free.

The balance of the fund that exceeds the Lifetime Allowance will attract a tax charge of 55% if it is withdrawn as a lump sum or 25% if it is left in the fund to be withdrawn as income.

Holly's pension income from both elements of her fund will be taxable at her marginal Non Savings tax rates.

If you have any further queries please do not hesitate to contact me.

Yours sincerely

Tax Senior

MARKING GUIDE

TOPIC	MARKS
Presentation and higher skills	1
Date final wages payment from Harry's Kitchens is taxable	1
Relocation expenses tax-free	1
Definition of ordinary commuting	1
No tax relief for costs of ordinary commuting	1
Travel to edge of geographical area is ordinary commuting	½
Travel within geographical area is in the course of the performance of Daniel's duties	1
Definition of a temporary workplace	1
Travel to head office is allowable	½
Mileage rates	1
How claim is made	1
Will still suffer NI on fuel allowance	1
Advise Daniel to ask employer to pay mileage instead	1
Conditions for gift to be exempt	1
Tax & NI implications if not exempt	1
Explanation of Lifetime Allowance & the level available to Holly	1
Fund split into authorised & non-authorised	1
Can take 25% tax free lump sum from authorised fund	1
Tax at 55% on any lump sum taken from the non-authorised fund	1
25% charge when starts to draw a pension from non-authorised fund	1
Tax treatment of on-going pension	1
TOTAL	**20**

ANSWER 5

	Non-savings	Savings	Dividend
	£	£	£
Employment income			
Salary	123,600		
Thank you payment (Note 1)	30,000		
Pension income			
UK pension income (Note 2)	1,500		
Foreign pension income (Note 3)	45,000		
Savings Income			
Bank interest		1,200	
Treasury Stock– 30/09/2018		750	
Treasury Stock– 30 March 2019 (Note 4)		500	
Treasury Stock – 1 April 2019 (Note 4)		500	
Japanese Government Bond (Note 5)		1,000	
Premium bond (Note 6)		-	
Non-reporting offshore fund (Note 7)		-	
Reporting offshore fund – Interest (Note 8)		1,000	
Reporting fund - Excess reportable income		700	
Dividend income			
HIJ Limited dividend			10,000
Total income	200,100	5,650	10,000
Share loss relief (Note 9)	(53,938)		
Taxable income (Note 10)	146,162	5,650	10,000

Tax

Basic rate band (Note 11)	44,500	20%	8,900
	101,662	40%	40,665
	5,650	40%	2,260
	2,000	0%	0
	6,188	32.5%	2,011
	1,812	38.1%	690
Tax Liability			54,562
Less: PAYE (salary)			(35,620)
Less: PAYE (Pension)			(600)
Tax payable			**£18,306**

Notes:

1. The thank you payment is made in recognition for services performed and has been made on or in anticipation of retirement. Therefore this payment is taxable.

2. The 25% lump sum withdrawal from the UK pension scheme will be tax-free. The amount flexibly withdrawn in March is taxable as non-savings income

3. As per s574A ITEPA 2003, for a lump sum payment, only growth in value since 6 April 2017 is chargeable to Income Tax in the UK.

4. Accrued income scheme will apply as the nominal value of the stock exceeds £5,000, which is above the exemption limit.

   Treasury Stock: March 19: £750 * 4/6 = £500

Treasury Stock: Annual interest -	£75,000 * 4% = £3,000
Payable 1 April 2019 -	£3,000/2 = £1,500
Less: amount relating period until 5 February 2019	£1,500 * 4/6 = -£1,000
Amount taxable as income on 1 April 2019	£500

5. The Japanese Government bond was issued at a discount of £1,000. This exceeds:

   0.5% * 10,000 (amount payable on redemption) * 10 (number of years) = £500

   Therefore this is a deeply discounted security and £1,000 is liable to Income Tax.

6. Premium bond encashment is exempt from tax

7. Income accumulated within a non-reporting offshore fund is not liable to UK income tax.
   The loss of £2,500 (£12,500 - £15,000) will be deductible from chargeable gains.

8. Reporting offshore funds are funds that have been approved by HMRC. Any income realised in the fund is taxable in the year it arises.

9. A loss on disposal of certain shares can be offset either against chargeable gains or income for the year of disposal, the previous tax year or both. The conditions that need to be met for this to apply is set out in s.131 ITA 2007.

   The amount of share loss relief that can be claimed is restricted by reference to the cap on unlimited income tax reliefs that applies where more than £50,000 in reliefs is claimed in a year. Gift aid is not included in this relief cap.

   The maximum relief that Rajesh can claim is the higher of 25% of income (£215,750 * 25% = £53,938) or £50,000.

   The loss realised on disposal of these shares amounts to £60,000 (£100,000 - £160,000). The remaining loss of £6,187 could be carried back to the prior year.

10. Due to the level of income received, the personal allowance is fully restricted.

    Rajesh is an additional rate taxpayer and therefore the savings allowance is not available.

11. Extension of basic rate band:

Gift aid	£8,000 * 100/80	£10,000	
Basic rate band		£34,500	£44,500
Original higher rate limit		£150,000	
Plus: gross gift aid		10,000	£160,000

MARKING GUIDE

TOPIC	**MARKS**
Calculation of general earnings from employment	1
Bank Interest	0.5
Dividend included as dividend income	0.5
UK pension income: Lump sum is tax-free Amount flexibly drawn taxable as income	 0.5 0.5
Foreign pension lump sum – Taxable only taxed on increase in value since 6 April 2017	 0.5 1
Accrued income scheme: £5,000 exemption doesn't apply Calculation of accrued interest on 3% Treasury Stock Calculation of accrued interest on 4% Treasury stock Inclusion as savings interest	 0.5 1 (0.5 for September amount, 0.5 for calculation) 0.5 0.5
Deeply discounted security: Identification Application of the formula to check if deeply discounted Taxable as income Inclusion in the savings income column	 0.5 0.5 0.5 0.5
Premium bond encashment – exempt	0.5
Offshore funds: Non-reporting fund – accumulated income not included	 1
Identification of loss being capital Reporting fund: Inclusion of interest paid out and accumulated income	0.5 1 (0.5 for each)
Share loss relief: Calculation of loss Operation of relief cap Identification that share loss relief is restricted	 1 1 0.5

Identification that gift aid is not restricted Carry back unutilised loss	0.5 0.5
Allowances not available Personal allowance fully clawed back Personal savings allowance not applicable	 0.5 0.5
Gift aid – gross up of gift aid Extension of bands	 0.5 1
Correct tax on NSI	0.5
Correct tax on SI	0.5
Correct tax on DI	0.5
Deduction of PAYE	0.5
TOTAL	**20**

ANSWER 6

To: Ted
From: Ms Tax Adviser
Date: 6 November 2019
Subject: Capital Gains Tax consequences of the offer for Woolly Ltd

Further to our recent correspondence with Agnes Wool, I have set out below the Capital Gains Tax (CGT) consequences of the offer for Woolly Ltd.

Option 1

	£	£
Cash paid immediately	100,000	
Cash paid over 3 years (Note 1)	300,000	
Cash paid if profit target met in 5 years (Note 2)	200,000	
Total proceeds		600,000
Base cost		(100,000)
Capital gain		500,000
Tax @ 10% (Note 3)		£50,000

Note 1 - The full proceeds of £300,000 would be treated as received immediately.

Note 2 - This is ascertainable deferred consideration £200,000 would be treated as received on completion.
If Woolly Ltd does not meet its profit target the excess tax paid can be reclaimed.

Note 3 - Woolly Ltd is a trading company, Agnes works in the business; her shares represent more than 5% of the voting rights and she has held the shares for more than 12 months. Agnes should therefore meet the requirements for Entrepreneurs' Relief (ER).

The date of disposal is the completion date rather than when the consideration is received. The payment deadline for any CGT due would be 31 January 2021.

Option 2

The "share-for-share" rules in s.127 TCGA 1992 will apply automatically to the Garment plc shares and this element of the consideration would not be immediately chargeable. It is unlikely that Agnes will meet the conditions for ER on a future sale of the shares as she will own less than 1% of the shareholding.

It is possible to make an election under s.169Q TCGA 1992 to dis-apply the share-for-share rules. The election must be made within 12 months of the 31 January following the year of the share exchange i.e. 31 January 2022.

The benefits of the election are that ER will apply to the gain and the base cost of the Garment plc will be higher on a future sale. However, the election will create an immediate charge to CGT even though Agnes has not received any cash proceeds.

I have shown two CGT calculations, with and without the election being made.

<u>CGT calculation where no election under s.169Q TCGA 1992 is made</u>

	£	£
Cash paid immediately	100,000	
10,000 shares	-	
5% of Woolly profits for the next 5 years (Note 1)	200,000	
Total proceeds		300,000
Base cost	(300,000/600,000 x £100,000)	(50,000)

Capital gain	250,000
Tax @ 10%	£25,000

The base cost of the Garment plc shares will be £50,000.

CGT calculation if an election under s.169Q TCGA 1992 is made

	£	£
Cash paid immediately	100,000	
10,000 shares	300,000	
5% of Woolly profits for the next 5 years (Note 1)	200,000	
Total proceeds		600,000
Base cost		(100,000)
Capital gain		500,000
Tax @ 10%		£50,000

The base cost of the Garment plc shares will be £300,000. The potential future saving on a future sale of the Garment plc shares, based on a future CGT rate of 20% is £25,000 ((300,000 – 50,000) x (20-10))

Note 1 - This is unascertainable consideration as the receivable is not known on completion. Therefore, the gain is calculated using the principal set out in *Marren v Ingles* [1980] STC 500.

Agnes will receive a chose in action and this must be valued on completion.

When Agnes receives the future consideration, there is a chargeable disposal of the chose in action and a chargeable gain or loss will arise at this point. The base cost of £200,000 will be deducted from the consideration to calculate the gain or loss. ER will not apply to this disposal and any gains will be taxed at 20% (if Agnes continues to be a higher rate taxpayer.)

If Agnes receives less than £200,000, she can make an election to carry back the loss to the year in which the original gain arose. The election is for the entire loss to be carried back and must be made within one year of the normal filing date for the return year in which the loss arose.

The loss can also be set against gains of the year it is incurred with any excess carried forward as for any other loss.

If you would like to discuss Agnes's position further, please let me know.

Kind regards

T Advisor

MARKING GUIDE

TOPIC	**MARKS**
Date of disposal	½
ER available	1
Date CGT payable	½
Option 1 - Tax payable now on cash instalments	1
Ascertainable deferred consideration treatment	1
ER available on ascertainable deferred consideration	1
Treatment of future loss	1
CGT calculation	½
Option 2 – share-for-share rules	1
ER unlikely to be available on future sale of Garment plc shares	1
Election to dis-apply and pay tax now	1
Unascertainable deferred consideration / Marren v Ingles – amount received immediately	1
ER available on proceeds treated as immediately received	1
Future disposal of chose in action	1
ER not available on future gain	1
Election to carry back loss	1
CGT calculation	½
TOTAL	**15**