

Capital Gains Tax Revised to 18%

The Chancellor of the Exchequer yesterday announced that UK capital gains tax will be reformed by moving it to standard rate of 18% in the new financial year. So there will be no more differentiation between business and non-business assets (AIM stocks will therefore be taxed at the same rate as fully listed ones), and taper relief will be abolished. UKSA has long campaigned for a reform of capital gains tax as the system is now so complicated that individual investors have great difficulty in working out their tax liability and often have to pay professional accountants to do it for them. With the new system, it will be exceedingly simple.

Private investors will of course also probably benefit overall as they will no longer be paying tax at 40% on some holdings, although they may of course be paying tax at 18% instead of 10% on unlisted securities and AIM stocks. In addition, the artificial incentive to hold shares for a longer period to obtain taper relief will be thankfully abolished so you can make decisions on when to buy and sell solely on the merits of the transaction, and not need to look over your shoulder all the time to decide whether this is going to be taxed at one rate or another.

But we regret the scrapping of the indexation allowance on older investments and generally think it would be wiser to re-instate some form of indexation allowance, even if that meant that the tax rate might be slightly higher. It is wrong that you can be taxed on the apparent "profit" made on an investment held for many years, when much of the increase in value may simply be down to general inflation in prices.

There are also going to be some unintended consequences of this new regime. We will revert to the age when it was advantageous to turn income into capital, as the latter will be taxed at lower rates than the normal higher rate taxpayer might pay on income. So companies will find shareholders will prefer capital appreciation rather than dividends and such measures as share buy-backs may grow in popularity. Also collective investment vehicles will be structured so that interest or dividends are "rolled-up" and returned as capital.

Investors may also welcome the proposals to permit couples to use double the £300,000 inheritance tax allowance, although most intelligent people have already drawn up their wills to use the nil-rate band allowance on the first death, so this is not as generous a proposal as it first appears.

The lack of prior consultation on these proposals, the little information on the details, and the likely adverse impact on some groups are also of concern.

Roger Lawson, UKSA, 10/10/2007

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