

## The capital gains small disposal rule

*Julie Butler considers if it is still relevant after 6 April 2002.*

With business taper relief coming into full effect from 6 April 2002, provided the conditions are met, the benefit of claiming other capital gains tax reliefs which interact with the business taper relief calculation must be called into question.

One of these reliefs is the small part disposal of land under *TCGA 1992, s242*. Under *s242*, proceeds from a small part disposal of land (for example, to be used to finance new ventures) can be maximised by taking advantage of the relief. The transferor may claim that the sale of the land does not constitute a disposal where the following conditions are met:

- 1 the consideration does not exceed £20,000;
- 2 the total consideration for all transfers of land made by the taxpayer in the year in question does not exceed £20,000; and
- 3 the consideration does not exceed 20% of the market value of the entire holding at the time of the transfer.

If a piece of land were to be sold, for example, by husband and wife trading in partnership, it will be necessary first of all to check if their annual exemptions for capital gains tax can be used. It will also be important to look at the business

taper relief calculation. There could be strong advantages in not claiming the small disposal relief so as to secure a higher base cost for future use.

This is not an exact science. One would have to take into account such things as how the taxpayer's base cost might be used in future, and the fact that death is not a chargeable event. (If the intention was to hold the asset until death, it could be argued that the effect on the future base cost is irrelevant.) However, taxpayers who intend to make another disposal would have to look at how they could use the base cost, how it would interact with future taper relief etc. and a number of possibilities have to be considered.

The case of small disposal relief shows what a nightmare the tax planner faces. When looking at the combination of capital gains tax reliefs, volumes have been written on tainted taper and the like, and from 6 April 2002, when more beneficial rates of business taper relief are effective, there will be even more choices available to the tax practitioner.

In all these instances it will be very important for the tax practitioner to document fully the options given to the client and, above all, to be able to demonstrate that the taxpayer has been

clearly informed that the decision rests with him and that he is making the decision whilst being aware of all the facts.

From a practice management point of view, there has to be careful recordkeeping. Staff must be aware that ultimately the decision rests with the taxpayer and not the tax practitioner. All advice given (whether by telephone, by e-mail or at a meeting) must be evidenced, a costly process which must be built into the fee structures surrounding such calculations.

There are many clients who have fallen into a habit of needing to make business decisions very promptly and who demand almost immediate, over the telephone, advice – do I buy now, do I sell now, etc.? It will be very important for the practitioner to make sure the client realises that with the complexity of the capital gains tax reliefs there is no such thing as a quick, over the telephone answer, and the need for proper documentation, proper fee structures and proper decision making by the client are imperative.

### **JULIE M BUTLER FCA**

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## Retiring partners – should a farmer ever retire?

It has been said that farmers never retire; they just die. The tax consequences of the retirement of any partner should be very seriously considered. Ceasing to be a partner is the cessation of trading status and various reliefs that go with it including agricultural property relief and, in this case, favourable tax treatment of the farmhouse. It is important, however, to look at possible retirement before death (no matter how unlikely that seems) as it may be forced on the farmer, for example by illness.

Following the business property relief case of *Beckman v IRC* (2000) SpC 226, it would appear that a retiring partner ceases to have a direct, proprietary interest

in a partnership asset, including agricultural land. It was decided that the interest in the partnership (which qualified for business property relief) had been converted into a debt owed by the partnership which was no longer relevant business property.

So what are the alternatives?

Where the partnership is to continue to farm the land, it would seem sensible for the land to be out of the balance sheet so that it is not a partnership asset but is held personally by the partners as individuals. There are various ways in which this may be done, with appropriate adjustments being made in the accounts. The debt owing to the retiring

partner would be reduced accordingly and he would be left with an interest in agricultural property used for agricultural purposes by someone else.

The above strategy would not work in relation to the farmhouse or cottage in which the retiring partner lives, as the house would no longer be used for the purposes of agriculture. ESC F16 would not be of any help either, since this relates to retired employees, not partners.

The tax planning exercise may be taken further to involve a home loan scheme. For farmers this can be used where the farmhouse does not qualify

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## Binding Contract for Sale

No business property relief for inheritance tax is given if the property is subject to a binding contract for sale.

This will be a particular consideration if buy-out arrangements are in place. See Statement of Practice SP 12/80 Business property relief from IHT: 'Buy and Sell' agreements for circumstances in which *IHTA 1984, s113* might apply.

The Revenue view is that mere options to buy and sell (distinguishing options from obligations) will not trigger *IHTA 1984, s113*. However, there have been recent signs that the issue may not be completely clear-cut for capital gains tax (as distinct from inheritance tax) purposes: it may be prudent to have successive (and different) exercise periods for the put and call options respectively.

The other area of concern is partnerships and, in companies, shareholder agreements.

The Revenue consider that there is a binding contract for sale where partners or shareholder directors enter into an agreement under which, in the event of death or retirement of one of them, his personal representatives are obliged to sell and the survivors are obliged to purchase the interest of the deceased in the partnership or company.

It is important to review partnership agreements and to structure shareholder agreements in the light of this provision. Note the need to structure life assurance arrangements tax efficiently within the context of shareholder agreements.

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## Personal pension plans

Another week passes, and two more group personal pension plan (PPP) employee members are discovered. I wonder how many well-paid employees are members of Group PPP schemes, unaware of the 40% tax relief available for all such UK employees!

These employees seem to think they are in a Retirement Benefits Scheme, covered by *ICTA 1988, ss590-612*, instead of a personal pension plan covered by *ICTA 1988, ss630-655*. Are senior directors and payroll staff ignorant of this? It seems that some are. The pension salesman may highlight the extra tax relief available at the point of purchase, but these words are ignored by many taxpayers.

**Solution:** Challenge all new clients who say that their pension scheme tax relief is covered via the company's payroll; ask to see papers relating to their own pension contributions. This becomes particularly important, as defined-benefit retirement benefit schemes are gradually replaced by stakeholder personal pension schemes, in order to save the employer's cash.

**PETER CROWTHER ATII**

## Professional subscriptions

When preparing tax returns for employees and directors, practitioners should remember to consider the professional bodies to which their clients belong. Many organisations are approved by the Inland Revenue for the purposes of *ICTA*, section 201 and the full list is available from tax offices for £5. (Unfortunately, that list was last published in 1999 and there is no way (without making a speculative claim) to ascertain whether or not a body has been added to or deleted from the list.) Many of the obvious bodies are on the list – for example the Institutes of Chartered Accountants, the Law Society and the Chartered Institute of Taxation. However, also included are less obvious candidates such as the Institute of Directors and the Royal Society of Arts.

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## Tax and the Euro

Any tax or national insurance liability may be paid in euros by CHAPS, BACS, cheque (through a euro account) or cash (euro notes only). There are two Euro payment helplines – Cumbernauld (01236 783500) and Shipley (01274 539630). No charges will be passed on to the taxpayer, unless payment is drawn on an overseas bank account. However, the payment will be converted at the current rate of exchange, and the Revenue will not meet the risk of any currency fluctuation. If an overpayment results, repayment will be made in sterling. UK income tax returns must be completed in sterling. However, a UK company may prepare most of its tax computation in euros, but it would have to convert the final figures into sterling to complete its tax return. The exception is the capital gains computation which has to be calculated in sterling. ■

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for agricultural property relief and is the owner's home. It may be used to save inheritance tax (IHT) by removing the value of an individual's home from their taxable estate for IHT purposes, whilst enabling the individual to reside in the property, rent free, without falling foul of the reservation of benefit rules.

In summary, such a scheme can:

- ◆ remove the value of family home from IHT estate;
- ◆ the retired farmer can continue living in property without the need to pay rent;
- ◆ he can retain control of the property;
- ◆ it can be achieved without attracting IHT, CGT and Stamp Duty; and
- ◆ there is an immediate IHT saving.

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