Tax Planning in the Recession - Transferring Assets to the Next Generation

By Ian Wright

When transferring non business assets such as let-property to children a capital gain arises as a transfer of assets to a connected person is treated as though it is disposed at market value. With a depressed housing and stock market, now might be the right time to transfer to children thus avoiding higher taxes in later years. Capital gains tax on such transfers would chargeable at 18% after use of the annual exemption. Many portfolios are standing at a loss and as such no capital gains would be payable. The same could be said for certain buy to let property.

The tax saving from an inheritance tax point of view could be very good too.

If you made a gift now and then died in ten years the following could happen:

2009 transfer
MV on transfer of property to children £500,000
Less cost of property £200,000

Gain £300,000
Less annual exemption £ 10,100

Taxable gain £289,990 @
18% = £52,182

Death say in 2019
Value of property £ 0 (not in estate of
deceased as gifted to child)

IHT due @ 40% NIL

If you did nothing and died after ten years the following could happen:

No transfer in 2009

Capital gains tax due NIL

Death in 2019
Value of property £700,000

Maximum IHT due @ 40% £280,000

Increase in taxes due to no gift £227,818
(comparison to transfer in 2009)

Of course there are risks. Should you die within seven years of making the gift then part, if not the whole, of the asset will come back into your estate for IHT purposes. In a worst case scenario you can end up with a double tax charge of both capital gains tax and inheritance tax. The absolute worst case scenario is dying within three years of the gift. With so much inheritance tax potentially being saved this may be a risk worth taking.

If you did nothing and died within two years the following could happen:

No transfer in 2009

Capital gains tax due NIL

Death in 2011
Value of property £520,000

Maximum IHT due @ 40% £208,000

If you did do a transfer now and then died in two years the following could happen:

2009 transfer
MV on transfer of property to children £500,000
Less cost of property £200,000

Gain £300,000
Less annual exemption £ 10,100

Taxable gain £289,990 @
18% = £52,182

Death in 2011
Value of property £520,000
Less fall in estate after payment of CGT £ -52,182

Taxable estate £467,818

IHT due @ 40% £187,127

Total CGT and IHT £239,309

Tax loss £30,309
(compared to no transfer in 2009)

To put this ten year hypothetical situation into context you can risk paying an extra £30,309 in tax in order to save £227,818. The same principal would apply for shares.

Combining the Share Portfolio Loss with a Property Transfer

If you were to carry out both exercises as above, you could offset the capital losses made on the share portfolio against the capital gain made on the property transfer, reducing your capital gains tax liability. There is, however, a provision known as 'clogged losses' which restricts loss relief between connected persons, so any transfers to children which create a loss will be restricted to gains made between the same persons. In the ideal scenario one would create a loss with share disposals, which is not so hard to do these days, and then use that loss against the gain on transfer of property.