

TAX INSIDER LITE

Flipping MPs – How to Avoid CGT on Your Second Home

By James Bailey

TAX TIPS

- If your spouse died and left everything to you, so that none of their inheritance tax “nil rate band” was used (see the July 2008 Tax Insider for details), you can effectively double your own nil rate band on your death. There has been an exemption from IHT for armed forces personnel killed on active service since 1952, and before that the exemption was more complicated but available in many cases. If your spouse was killed in action HMRC’s “Inheritance Tax and Trusts Newsletter” for April 2009 (<http://www.hmrc.gov.uk/cto/newsletter.htm>) contains more detail on how this will affect your right to the “transferable nil rate band” and how to claim it.
- Are you liable to tax on “pre owned assets”? This is where you are taxed on a notional “rent” for assets you used to own and still have the use of, but have given away. Bear in mind that the tax is charged by applying the “official rate of interest” to the market value of the asset, and there is a de minimis exemption of £5,000. With the “official rate of interest” now down to 4.75%, your pre owned asset charge may have dropped below the de minimis level.

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There has been a great deal of excitement in the press about MPs “flipping” their properties in order to avoid capital gains tax on selling their second homes, but this is a game anyone with more than one “residence” can play. In view of the hysteria about this in the press, I should perhaps point out that it is perfectly legal tax planning!

The basic rule is that you are exempt from CGT on a gain from selling your “main residence”. You can only have one main residence at the same time (and if you are married or in a civil partnership, you can only have one between the two of you).

There is one exception to this rule - if a property has been your main residence at any time during your ownership of it, then this exemption extends to the last 36 months before you sell it, even if in fact you have another main residence during that period. The idea of the legislation is to take account of the fact that you may need to buy a new home before you manage to sell the old one, but it provides an opportunity for some useful tax planning.

If you have more than one “residence”, the law allows you to nominate which one is to be treated as your “main residence” for tax purposes and so enjoy the exemption from CGT. **You must do this within two years of it becoming necessary to decide which is your main residence.**

Once you have made this nomination, by writing to the tax office that deals with your tax affairs, you can subsequently vary that nomination at any time in the future, and the variation can be backdated by up to two years. In the case of a married couple or civil partnership, both must sign the nomination and any subsequent variation.

For example:

Joe lives in Devon with his family, in an old farmhouse. He gets a job in London, and buys a small flat there where he lives during the week. He (and his wife) writes to the tax office, nominating the farmhouse as their “main residence”.

Three years later, Joe decides to sell the London flat, which has increased in value by say £50,000. He and his wife write to their tax office and vary the nomination of their main residence in favour of the London flat, with effect from (say) 1 April 2009. A few weeks later, they write again, and vary the nomination back to the Devon farmhouse, with effect from 1 May 2009.

Because the London flat was properly nominated as their “main residence” for one month (April 2009), the last 36 months of the gain (so in this case, all of it) are exempt from CGT.

The Devon farmhouse has lost only one month of exemption, so if it were sold after they had owned it for ten years, only 1/120 of the gain would be taxable, and that would almost certainly be covered by their CGT annual exempt amounts (£10,200 each for 2009/10).

If you are keen to learn more, here are the other articles that feature in the Tax Insider magazine this month:

- **The Bad Tax Scheme Guide - HMRC Puts Tax Avoiders on Notice!**

By James Bailey

James discusses the disclosure of details about tax avoidance schemes used by professionals, and HMRC's new, recently published, information sheet "Spotlights".

- **Get it in Writing!**

By Mark McLaughlin

Mark reveals how pitfalls can sometimes appear when exploiting loopholes in the law due to unreliable advice provided by HMRC in certain cases.

- **Tax-free B & B**

By Sarah Bradford

Sarah looks at the possibility of earning a little extra cash by renting a spare room in your home, either to a lodger or on a bed-and breakfast basis.

- **Disappearing Tax 'Secret'**

By Mark McLaughlin

Mark reveals the 'secret' tax treatment that could prove very helpful, but is available for a limited period only.

- **Company Directors Converting Part of Their House into an Office - Reclaim the VAT!**

By Andrew Needham

Andrew reveals the rules on claiming VAT on the conversion costs incurred when working from home, and how you can go about reclaiming that VAT.

- **How to Pay off Your Residential Mortgage and Claim Interest Relief**

By Arthur Weller

Arthur shows how it is possible to claim interest relief on properties that do not form part of your rental business i.e. your main residence.

Your Question Answered by Arthur Weller

Q: Can you advise or point me in the right direction. I am buying an investment property with my son and he will be living in it. I am loaning him half of the purchase price. What would be the tax implications when I sell in 3-5 years as it would be his PPR but not mine?

A: If the property is in your son's name, i.e. he is not only the legal owner but also the beneficial owner, then when the property is sold 3-5 years from now there will be no capital gains tax because your son (I assume) has lived in it all the period of ownership. If you own half the property, then only he will get PPR relief on his half, but you will not get any relief on your half. If you own the whole property then no PPR relief will be available at all.

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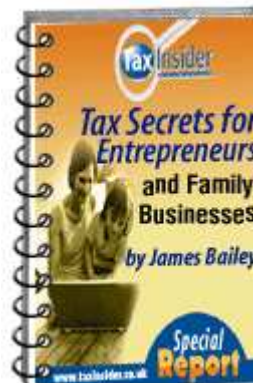
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