

AF1 Capital Gains Tax.2023/2024

Part 2: Dealing with losses.

The milestones for this part are to understand:

- How to deal with a loss and a gain in the same tax year
- How to deal with a carried forward loss
- How to deal with a mixture of residential and non-residential losses

Losses

Since CGT taxes gains or profits on the disposal of an asset it follows that any losses can be offset against gains. As with gains, losses can only be offset when the loss is realised. There is an exemption for shares of negligible value. These are shares in companies that have either gone into liquidation or ceased trading and there is no market for them. HMRC publish an official list of these and a claim for disposal can be made without selling shares on this list.

Losses made on assets exempt from CGT such as directly owned Gilts and Bonds cannot be offset.

If a loss and a gain are made in the **same tax year**, the rule is that the **total loss must be deducted from any gain before the annual exemption is deducted**.

Sandra has made a gain of £15,000 and a loss of £10,000 in the same tax year. This reduces the loss to £5,000.

Gain	£15,000
Loss	<u>£10,000</u>
Adjusted Gain	£5,000

Because it is below the annual exemption no tax is payable but it's not tax efficient. Ideally she should just offset £9,000 of the loss to bring the gain down to £6,000 and carry forward £1,000 to future years. Unfortunately, HMRC don't allow this.

However if there is a **carried forward loss**, that is a loss incurred in an earlier tax year:

- the annual exemption is first offset against the gain
- then all or part of the carried forward loss can reduce the gain to zero with any unused loss being carried forward to future years.

David has a gain of £18,000 in the current tax year and has £15,000 losses from previous years

Gain	£18,000
Less Annual Exemption	<u>£6,000</u>
Gain	12,000
Less carried forward loss	<u>12,000</u>
Chargeable Gain	0

Remaining carried forward loss £3,000

Carried forward losses can be created in two ways:

- Charles has made a gain of £12,000 and a loss of £20,000 in the same tax year. The loss wipes out the gain and the remaining £8,000 can be carried forward to another year.
- Anne made a loss of £20,000 without crystallising any gains in the same tax year so the whole amount can be carried forward.

Losses can be carried forward indefinitely but HMRC must be notified of a loss within 4 years of the loss occurring even though it is not claimed at that time.

If there is a loss and a gain in the same tax year and losses to carry forward the process is as follows:

- The whole of the current year's loss must first be offset against that year's gain
- If there is still a gain, the annual exemption of £12,300 would be deducted.
- If there is still a taxable gain all or part of the carried forward loss can offset to further reduce the gain.

Kate made a gain of £20,000 and a loss of £6,000. She also has a carried forward loss of £13,000.

Gain	£20,000
Loss (current year)	<u>6,000</u>
Taxable gain	14,000
Less Annual Exemption	<u>6,000</u>
Chargeable gain	8,000
Less c/f loss	<u>8,000</u>
	0

Previous loss	£13,000
Less	<u>8,000</u>
Loss to be carried forward	£5,000

Interaction of Residential Property and other gains.

As noted earlier, CGT on residential property is charged at 18% and 28%. When an individual has disposed of residential and "ordinary" property in the same year this adds an additional layer of complexity. Look at this situation.

Emil, a higher rate tax payer made a gain of £40,000 on some shares and a gain of £60,000 from residential property. Against which gain should the annual exemption be offset?

HMRC allow the annual exemption to be offset against the property gain

Residential Property Gain	£60,000
Less annual exemption	<u>£6,000</u>
Gain	£54,000
Gain on shares	<u>£40,000</u>
Total gain	£94,000

This is beneficial because the amount that is taxed at 28% is reduced. Similarly, a loss on other assets can be offset against residential property.

Tom makes a gain of £50,000 on the disposal of a residential property gain. He sold some shares for a gain of £15,000 but made a loss of £10,000 on some other shares.

Property gain	£50,000
Less share loss	<u>£10,000</u>
	£40,000
Less annual exemption	<u>£6,000</u>
Gain	£34,000
Plus share gain	<u>£15,000</u>
	£49,000

If Tom is a higher rate tax payer then £34,000 would be taxed at 28% and £15,000 at 20%.

However, suppose Tom was retired and has £18,000 of his basic rate band left, is the lower rate of CGT applied to the property or share gain? The HMRC rule is that the lower rate is applied to the non-property gain.

Share gain	£15,000 @ 10%	£1,500
Remainder of basic rate band (£3,000)		
Property Gain (£34,000)	£3,000 @18%	£540
	£31,000 @ 28%	<u>£8,680</u>
		£10,720

To sum up these rules. Where both a property and non-property gains have been made:

- The annual exemption can be offset against the residential property gains.
- Losses on non-property gains can be offset against property gains
- If the individual's income has not used up all their basic rate band, the lower rate of CGT must first be charged on the non-property gain.

That concludes this part so you should now understand:

- How to deal with a loss and a gain in the same tax year
- How to deal with a carried forward loss
- How to deal with a mixture of residential and non-residential losses