Your Legal Questions

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CGT Reliefs for individual business owners Part 5

This week we consider Roll-over relief ("ROR") on the incorporation of an existing business.

Q. What is Roll-over Relief?

A. See our article on 12th August 2010 for a detailed explanation about ROR but essentially the relief is designed to allow Capital Gains Tax ("CGT") on the disposal of an asset to be postponed to a later date.

Q. How does ROR apply on incorporation?

A. When a business is transferred by a sole trader or partners into a company a disposal occurs for CGT purposes and tax would be payable. ROR allows payment to be deferred providing qualifying conditions are met.

Q. What are the conditions for the relief to apply?

A. The business must be transferred as a going concern so that it is essentially the same business but run by the company instead of the sole trader or partners. The consideration or payment for the business must be in the form of shares issued by the company. Other than cash all of the assets of the business must be transferred to the company.

Q. How does the relief work?

A. The gain on the disposal of the business (i.e. the amount by which the business increases in value during the period of ownership by the sole trader or partners) will be rolled over by notionally deducting it from the acquisition cost of the shares. If the business is valued at £100,000 including a chargeable gain of £25,000 and is transferred in exchange for £100,000 worth of shares then the acquisition cost of the shares for CGT purposes will be £75,000 (£100,000 less £25,000). This will be the base cost when calculating any gain on a subsequent sale of the shares in the company.

Q. Does the relief automatically apply?

A. Yes, unless you choose not to use it. In some circumstances it is better to pay the CGT on incorporation rather than to defer it. Professional advice is essential.

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