

Capital Gains Computations

The most likely tasks in this area fall into the following groups:

- ☞ Calculating the gain on disposal of a business asset by an individual
- ☞ Dealing with the disposal of shares by limited companies
- ☞ Dealing with partial disposals
- ☞ Dealing with business reliefs

Calculating the Gain on Disposal of a Business Asset by an Individual

When an asset is disposed, the capital gain or loss is calculated as follows:

Disposal value (less incidental disposal costs)	XXXX
Less allowable expenditure (including enhancement expenditure)	(XXXX)
Gain/loss	----- XXXX -----

This basic calculation applies to both individuals (who pay capital gains tax) and companies (who pay corporation tax), but a few points are worth mentioning.

Indexation allowance started in April 1982, as an attempt to allow for inflation. In other words, an attempt to avoid the taxation of gains which are purely due to inflation. An indexation factor is calculated based on changes in the retail price index, and the allowable expenditure is multiplied by this factor to arrive at the indexation allowance, which is then deducted from the gain calculated above.

The indexation factor is calculated as follows:

$$(RD - RI) / RI$$

where RD is the RPI on the date of disposal and RI is the RPI on the date the expenditure was incurred. The indexation factor is rounded to 3 decimal places, and must not be used to create or increase a loss (in other words, if the calculation results in an unindexed loss, no indexation allowance is allowed. If the calculation gives an unindexed gain of £400, the maximum indexation allowance allowed is £400).

Indexation allowance applies to companies, but NOT to individuals.

(Prior to 6 April 2008, individuals were allowed indexation allowance up to April 1998 and taper relief thereafter, but both have now been abolished).

Dealing With the Disposal of Shares by Limited Companies

When a holding of shares has been built over the years by a number of purchases, and part of that holding is sold, matching rules are needed to determine precisely which shares have been sold.

For limited companies, the matching rules are as follows:

First	acquisitions on the same day
Then	acquisitions in the previous 9 days (FIFO basis)
Then	shares in the s104 holding (acquired since 1 April 1982)

In fact there are rules going back further than this, but the examiner has made it clear that questions will not involve any acquisitions prior to 1 April 1982.

The rules mean that any shares which are not sold within 9 days of purchase will be put into the s104 holding or pool. Here they lose any individual identity. The pool operates as follows:

- ☺ Pool records must be kept to show the number of shares, their original cost and the indexed cost
- ☺ Whenever shares are bought or sold (an operative event), the pool must be indexed up to date first
- ☺ This indexing IS necessary for a rights issue, but NOT for a bonus issue (since this is regarded not as a new issue but simply as a reorganisation of existing capital)

Note that within the pool, the indexation factor does not have to be rounded to 3 decimal places.