Tax efficiently selling down a Buy-To-Let property portfolio

Lara is a buy-to-let landlord who originally purchased one of her properties for £400k and will sell it for £500k. This creates a taxable capital gain of £100k, and a £24k* capital gains tax (CGT).

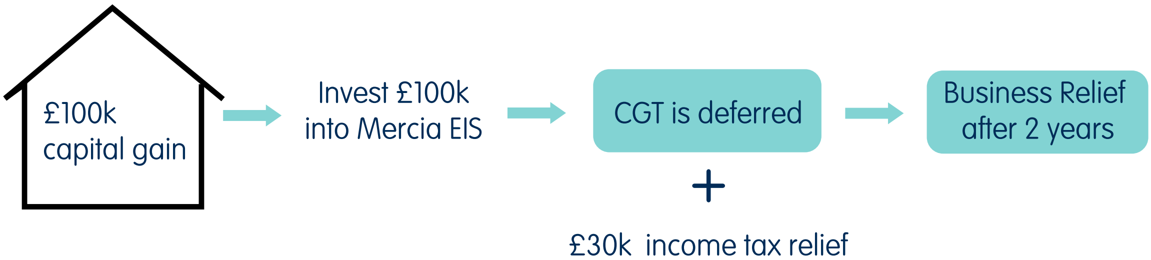
Lara has a large property portfolio which she is thinking about slowly selling down. She wants to test an EIS strategy before committing to additional EIS investments.

- Her annual income is £90,000
- She has significant wealth within pension & ISA and uses her allowances for both each year as well as her CGT allowance.
- She has a significant capacity for loss, as she has £500k of cash savings.
- She is prepared to invest for the long term, as she does not need the capital.

Lara's financial adviser recommends an EIS to defer her capital gain, whilst also taking advantage of income tax relief.

As well as the income tax relief Lara will benefit from, she will not pay any capital gains tax on her £100k profit until the EIS exits, or even indefinitely if she continues to re-invest.

In addition, any gain from the EIS investment is not liable for CGT.** After two years, the investment becomes eligible for Business Relief and is taxed at 0% for inheritance tax.



On exit, the original gain will recrystallise and be taxed at the prevailing rate

If she wishes to pay the tax bill, Lara may have offset the impact of the tax through growth in her EIS. The companies within her portfolio aim to be all sold within 5-7 years, meaning the gains may reappear across multiple tax years.

She may be able to reduce the amount of CGT she pays using the CGT allowances available in the years that the gains reappear.

Likewise, if Lara wishes to reinvest the EIS sale proceeds to re-defer the gain, she may be able to reduce the amount she needs to reinvest using her CGT allowances.

Over the years the gain may be whittled away, or finally disappear on death. At the same time, Lara potentially has built a rapidly growing asset that provides income tax relief with each re-investment and will qualify for Business Relief (if held for two years).

*After the March 2024 budget, the CGT rate on property has been reduced to 24% from 28%. If you have a client with a gain incurred before March 2024 and within three years, even more CGT can be deferred.

** Providing the shares have been held for at least three years, income tax relief has been claimed and not withdrawn, and no qualifying conditions have been breached.

*** Providing the tax rate has remained the same as 2024/2025. Tax treatment depends on the individual circumstances of each client and may be subject to change in future.

EIS Tax Planning with Mercia | how advisers can achieve attractive tax advantages for their clients

EIS allows investors to gain exposure to high-growth British SMEs, whilst also benefiting from very attractive tax reliefs.

EIS tax reliefs are designed to give investors an added incentive to support smaller, entrepreneurial businesses with the benefit of an asymmetrical return profile in the form of downside protection and tax-free growth.

Investors that may benefit from the below tax reliefs may wish to consider an EIS investment. If an individual can benefit from more than one relief, the rationale for an EIS investment will be even stronger.

Mercia's minimum subscription is £25,000. The maximum investment for income tax relief is £1m in any tax year or £2m if the additional investment is made into Knowledge-intensive companies.

Mercia also offers an approved Knowledge Intensive (KI) Fund once a year, and always has a tranche of its main EIS fund open.

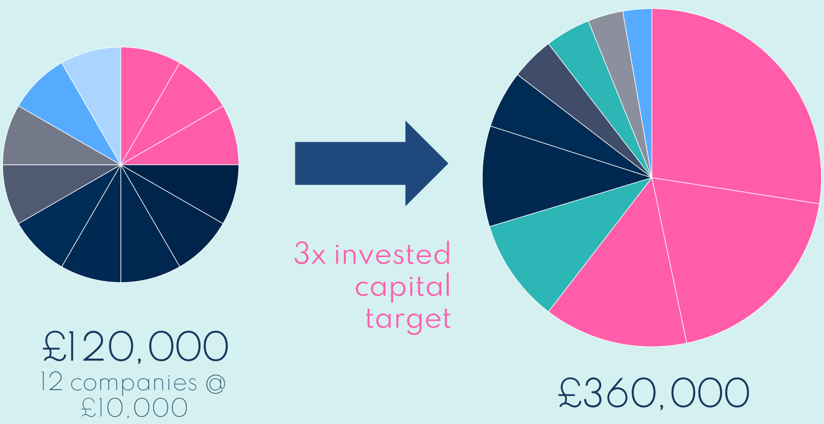
Tax incentives available

- Income Tax Relief - 30% income tax relief is available until the investor's income tax bill is reduced to zero.
- Capital Gains Tax (CGT) deferral - which can be used to manage a CGT liability. For example, when selling a business, a second home or a share portfolio.
- Inheritance Tax Relief - An investment into an EIS fund typically qualifies for Business Relief, reducing the inheritance tax to 0% for these assets.

Tax-free growth and downside protection

- Tax-free gains - if EIS shares are sold for more than was paid for them, any profits are free from capital gains tax.
- Loss relief - We expect a third of portfolio companies to fail (see image below) and when this happens investors can offset any loss against their income tax (or capital gains tax) liability.

Mercia EIS model portfolio*



The BIG Winner #12 (10x)	£100,000
Winner #11 (7x)	£70,000
Winner #10 (5x)	£50,000
Income tax relief	£36,000
Company 9	£30,000
Company 8	£20,000
Company 7	£16,000
Company 6	£12,250
Company 5	£10,000
Loss relief on companies 1-4	£15,750

*Please note that this model is not guaranteed and should only be used for illustrative purposes. It does not include any benefits from CGT deferral or IHT reliefs.

Risk warnings

Don't invest unless you're prepared to lose all the money you invest. This is a high-risk investment and you are unlikely to be protected if something goes wrong. EIS investments are restricted to high net worth or sophisticated individuals, or those advised by a qualified financial adviser, per FCA rules. Evidence of qualification is required with your application. Tax treatment depends on the individual circumstances of each client and may be subject to change in future. Read the full risk warnings in the Fund documentation before applying. Past performance does not predict future results. These investments are illiquid and may lack a readily available market for selling. Investments in non-Sterling currencies may be affected by exchange rate changes. Mercia Fund Management Limited, a subsidiary of Mercia Asset Management PLC, is the EIS fund manager and authorised and regulated by the FCA (FRN: 524856).

Take 2 minutes to learn more.