Avoiding tax could prove costly

Colm Fagan **Diary of a Private Investor** **Update 19** **24 October 2019**

A decision not to sell, in order to avoid a hefty tax bill, proves questionable in light of subsequent events.

Anyone who claims to get all, or nearly all, their investment calls right is a liar. Experience over many years has taught me that it's impossible to time the market or individual shares, except on the very odd occasion. Investing is a constant roller-coaster of fear and hope. Sometimes those fears and hopes are justified by subsequent events, oftentimes not. I consider myself lucky if I get 70% of my calls right. I doubt if anyone, even Warren Buffett, arguably the best investor of our time, can hope to achieve a success rate much above 75%.

My recent experience with Renishaw, the UK-quoted metrology company, illustrates the point. In mid-2018, things were looking good for Renishaw and my shareholding in it. The company's share price was well north of £50, more than double what it had been only two years previously: at end June 2016, it was as low as £21.40. Renishaw was my largest shareholding by a distance, valued a third more than my next biggest investment, Phoenix Group Holdings.

In mid-summer 2018, I experienced a touch of vertigo and sold just over 10% of my holding at an average £56.21 a share. My timing was good. The price fell in the following weeks and months as the wonderful summer of 2018 turned to autumn. In September, I decided the price fall had been overdone. I bought back around a third of what I'd sold just a couple of months previously, at what I thought was a bargain basement £51.13 a share. How wrong I was.

By the end of October last, storm clouds had gathered for Renishaw's business and I had changed from being a summer bull to an autumn bear. The proximate cause of my change of heart was fear of a slowdown in China, one of Renishaw's biggest markets, coupled with the looming prospect of an international trade war and fading hopes of an orderly Brexit. As nearly always in such circumstances, I was not alone. Other investors shared my fears. They were reflected in the share price, which fell from over £50 at end September to less than £40 a month later. I was now more bearish than the market. I believed the price could fall further, so I decided to cut my holding, even though it meant swallowing my pride and taking a heavy loss compared to recent highs.

Starting in late October 2018, I sold all the Renishaw shares in my tax-exempt pension accounts, and some in the taxable (non-pension) account, at an average £40.25 a share. It was a far cry from the £51.13 at which I had added to my holding only a short time previously, but I've learned, often the hard way, that life as an investor is a constant litany of missed opportunities, brightened by the occasional coup. I am now, finally, close to a state of serenity that allows me "to treat those two impostors just the same."

I held off selling any more from my taxable account, because it would result in a hefty Capital Gains Tax (CGT) charge, on top of the one I had already incurred after the partial sale from the same account. In Ireland, Capital Gains Tax is charged at 33%, which is high by international standards: in the UK, the most I would have had to pay is 20%. The shares I was prepared to put on the chopping block only cost £15.90 apiece when I bought them back in 2013, so selling at £40 would have resulted in a CGT liability of almost £8 a share. (I'm ignoring the complication caused by the requirement to convert both purchase cost and sale proceeds to Euros at the exchange rates ruling when the transactions were completed.) I didn't want to give that much away to the taxman (or woman!) so I decided to hang on.

Earlier this month, the Renishaw share price fell briefly to under £32.50 after a profit warning, caused – you've guessed it – by lower sales, especially in China. The price fall made me question my decision to hang on when the price was higher. CGT must be paid eventually, so maybe I should just have taken my medicine when I thought the company was overvalued and moved on.

It's too late now to apply that lesson. I no longer have strong views on whether Renishaw is undervalued or overvalued by the market. Even after the recent sales, it is still my second-biggest holding. If there were no CGT, I would probably reduce my holding in the interests of diversification, but the prospect of having to pay a hefty tax bill – over £6 a share at the current share price – is a major deterrent.

It makes me wonder if the government's finances would be improved by cutting the CGT rate. This would encourage more people to make buy and sell decisions on economic grounds rather than for tax reasons. This could deliver better results all round: more value-adding transactions and higher tax revenues for the state, despite a lower tax rate. It's interesting to note that the Irish government's take from Capital Gains Tax in 2005, when the rate was 20%, was around twice as much as it hopes to collect this year, when the rate is 33%. I realise that this is far from convincing proof of my thesis, but it's interesting, nonetheless.

Of course, I could hang on until I die, at which point there would be no CGT, but where's the fun in that?

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