PRIVATE TREATY SALES: GUIDANCE
Published 21 October 2022

Introduction

1. Private treaty sales of pre-eminent works of art to most public collections are exempt from capital taxation (Inheritance Tax and Capital Transfer Tax by virtue of sections 32(4)(a) and 32A(5)(a) of the Inheritance Tax Act 1984; Estate Duty by virtue of the proviso to section 40(2) of the Finance Act 1930; and Capital Gains Tax and Corporation Tax by virtue of section 258(2) of the Taxation of Chargeable Gains Act 1992).

2. This is an important and attractive exemption for both buyer and seller and applies to pictures, furniture, manuscripts and a wide range of other heritage items which have either been granted exemption from capital taxation in the past or, if not, satisfy the criteria of pre-eminence on which conditional exemption is based. Guidance on the interpretation of pre-eminence in respect of objects is at Note B below and they may help you to assess whether a particular work of art or other object is likely to meet the criteria.

3. For an agreed valuation, a private treaty sale will usually be more fiscally advantageous to the owner of a work of art than an open market sale on which tax is paid. This can be so even if the object has not previously been granted exemption from capital taxation. In that case, if a private treaty sale were in prospect HM Revenue & Customs (HMRC) would look to the Arts Council for advice on whether the property met the requisite standard.

4. The purchasing institution, usually a national or local museum, gallery or library, will also benefit from the arrangement. Qualifying purchasing bodies for these purposes are listed in Schedule 3 of the Inheritance Tax Act 1984 and called Schedule 3 bodies. A list of them is at Note A below. (Note: The range of bodies is more limited when the private treaty sale is of an object which was granted exemption from Estate Duty: for further information on these please contact the Arts Council.)

5. HMRC has confirmed that it is acceptable for a Schedule 3 body to “front” the purchase on behalf of a non-Schedule 3 acquiring institution dependent upon the latter’s suitability and on its preserving the property for public benefit. For more details please contact the Arts Council.

6. Some of the information in these guidelines appears in HMRC’s guidance *Capital Taxation and the National Heritage.* It is repeated here for ease of reference.

Advantages of a private treaty sale

7. If you are the owner of a heritage work which you now wish to sell, you may think that you will get your best return by an open market sale. But a private treaty sale to a qualifying public collection frequently offers a more certain return, taking into account the tax liability to which you may be subject.

8. If a work of art is sold in the open market the vendor may be liable to one or more of Inheritance Tax or one of its predecessors, Capital Gains Tax and Corporation Tax. However these tax charges are **not** incurred where an owner sells by private treaty to a qualifying body. The transaction is entirely tax free. The tax exemption is shared between the vendor and the acquiring institution by what is known as the *douceur* arrangement (see paragraph 10 below).

9. Not only will such a private treaty sale normally be of greater benefit to the owner than an open market sale that entails payment of capital taxes, but a private treaty sale will also enable the vendor (with the help of the acquiring institution) to ensure that a part of our national heritage is retained in this country.

The *douceur* arrangement

10. While the vendor receives the proceeds without any liability to tax, it is not unreasonable that the acquiring institution should offer, and the vendor be prepared to accept, a lower price than would prevail if the proceeds were taxable. In this way the vendor and the acquiring institution share the value of the tax exemption. The *douceur* arrangement, which is administrative not statutory, is designed to reflect this and to enable both parties to negotiate on a firm basis. The *special price* for the transaction, which takes account of the tax exemption, is arrived at by adding to the notional after-tax value of the heritage object a percentage (normally 25%) of the notional tax liability. This addition to the net value is known as the *douceur*.

11. The rate of douceur is flexible, although prospective purchasing institutions will normally think in terms of 25%. A higher figure may be appropriate to provide an adequate inducement in respect of low value items or where the tax liability is relatively small. A lower figure may be appropriate in respect of an item of high value: this could still be attractive to the vendor, and could bring it within the financial compass of a public purchaser.

12. The table below shows how a private treaty sale price would be calculated on the basis of a 25% douceur. In this case, the seller would receive £11,200 more than if they had sold their work of art on the open market at the same price as the agreed value and paid tax to HMRC.

Calculation of the special price for a private treaty sale: douceur at 25% subject to negotiation.

Agreed current market value, say			£100,000
Tax applicable:			
	CGT at 20% on gain element assumed to be £40,000	£8,000	
	IHT payable at 40% on £92,000 (market value less CGT)	£36,800	
Total tax			-£44,800
Net receipts after full tax			£55,200
Add back 25% of total tax (the douceur)			£11,200
Tax exempt price payable by the acquiring institution (the special price)			**£66,400**

The sum of £66,400 is known as the special price. It is what the vendor receives from the public collection; any dealer's or auctioneer's commission must also be met from it.

- The vendor has £11,200 more than if they had sold the object for £100,000 on the open market and paid the tax.
- The public collection pays £66,400 which is £33,600 less than its agreed open market value.
- HMRC does not collect £44,800, the total tax that it would otherwise have received.

13. Costs of sale, such as professional fees, are **not** taken into account in the notional tax calculation and therefore have to be met from the sale proceeds. But by opting for a private treaty sale the vendor does **not** incur a seller's premium.

14. Because such sales are exempt from Capital Gains Tax (CGT), other CGT reliefs are not normally available. Thus, for example, loss relief or rollover relief for the replacement of business assets is not applicable and is not taken into account in working out the special price. Nor is one's annual exemption. Some reliefs, however, such as the chattels' exemption and principal private residence relief are normally taken into account. HMRC should be consulted in cases of doubt. Rarely a vendor's tax affairs might militate against a private treaty sale. This would depend on the arithmetic.

(Note: the douceur does not apply if a Schedule 3 body purchases the object at a public sale, e.g. at auction. It is limited to sales by private treaty.)

15. There may also be other advantages to the vendor from a private treaty sale and these are listed at paragraph 10.4 of HMRC's guidance. Most notably:

A gift by X of a pre-eminent work of art to B might be a potentially exempt transfer. If B sold the work by private treaty to a Schedule 3 body within 7 years after that gift, section 26A of the Inheritance Tax Act 1984 would render it an exempt transfer.

Assume X wishes to pass on cash to their children or grandchildren. They have a pre-eminent work of art and have agreed to sell it to a Schedule 3 body. Instead of selling it themselves and passing on some or all of the proceeds (which might leave the gift vulnerable to tax if they were to die within seven years of making it), they transfer the work of art or a share in it to the desired end recipients immediately before the private treaty sale is completed. In this way they will be able to pass on the sale proceeds entirely tax free with no possibility of this gift becoming chargeable in the event of X's death within seven years. If the work of art is subject to a previous exemption HMRC agrees to *telescope* the transaction and ignore the in-between stage as the exemption could have been continued and the undertaking to preserve and allow public access is dispensed with on the understanding that the work of art will at once become the property of a Schedule 3 body. The same applies to Capital Gains Tax: the gift in-between is ignored as it could be held over under section 258(3) of TCGA 1992. The notional CGT will be reckoned with X as the relevant person in assessing the special price.

16. Private treaty sales to Schedule 3 bodies are relieved from VAT (Group 11, Schedule 9 of the Value Added Tax Act 1994). Information about this is given in VAT Notice 701/12 - Disposal of Antiques, works of art etc. from historic houses.

17. For further details on these schemes and how they work and for guidance on how private treaty sales work in the case of export-deferred items please contact the Arts Council or the Heritage Team at HMRC.

Steps to be taken by an owner

18. If you are interested in a private treaty sale the steps to be taken are listed below:

- First, approach the museum or gallery of your choice (or any other body listed in Note B) and ask them whether they are interested in acquiring your work of art.
- Once you have identified a prospective buyer, propose a current open market value for your work of art and on this basis negotiate a valuation acceptable to both parties. It may be in your interest to seek professional help on valuation and to identify and negotiate with potential purchasers;

the Arts Council can also advise on suitable purchasing institutions and those most likely to be interested in acquiring your work of art.

- Next, negotiate the current and, if necessary, historic value of the work of art and agree the special price to be paid for the object under the douceur arrangement. **In considering the special price, the potential purchaser will always need to know how the calculations will be affected by the vendor's tax position.** HMRC should therefore be authorised to disclose information relevant to the sale - on a strictly confidential basis - to the purchasing institution.
- When agreement has been reached on the special price, HMRC will be asked - usually by the vendor - to check the *douceur* calculation.
- As soon as HMRC has agreed the figures and confirmed to both the vendor and the acquiring institution that the transaction will be tax free the sale can be completed.

19. If a prospective vendor does not give their consent for HMRC to be consulted about their tax position, the institution should seriously consider withdrawing from the negotiations. Failure to do so could result in a much higher price being paid for the object than is reasonable in a tax exempt transaction. This would be an unacceptable use of public money.

Advice to acquiring institutions

20. When approached by a vendor, the prospective purchasing institution should always seek to arrive by negotiation at a fair market price for the work of art. **The institution should never start from a figure conditioned by its own resources. If what would be a fair market price appears to be beyond its own means the institution should explore the possibility of supplementary funding from other sources**. Further advice on potential funding bodies can be obtained from the Arts Council. Alternatively, it could consider a joint purchase with another institution.

21. In order to satisfy itself that the rate of douceur it is offering is realistic and that it is acquiring the object for a fair price, **the institution should consult the Heritage Team at HMRC, with the vendor's consent, during negotiations of the special price and before the transaction is concluded.**

Land and buildings

22. Private treaty sales of outstanding land and historic buildings can also be made to any of the bodies listed in Schedule 3. The approach is similar to that for objects, except that, because neither buildings nor land can normally be exported, 10% rather than 25% of the value of the tax exemption will normally be used in the calculation of the special price.

Conclusion

23. **Private treaty sales of heritage items offer appreciable advantages to both parties.**

24. Works of art of pre-eminent quality and outstanding land and historic buildings may also be offered to the government in settlement of inheritance

tax, capital transfer tax or estate duty liabilities. Guidance on acceptance in lieu is available on the Arts Council's website and in Chapter 11 of HMRC's guidance.

BODIES WHICH ARE ELIGIBLE TO NEGOTIATE A PRIVATE TREATY SALE

The National Gallery. The British Museum. The National Museums of Scotland.
The National Museum of Wales. The Ulster Museum.

Any other similar national institution which exists wholly or mainly for the purpose of preserving for the public benefit a collection of scientific, historic or artistic interest and which is approved for the purposes of this Schedule by the Treasury.

Any museum or art gallery in the United Kingdom which exists wholly or mainly for that purpose and is or has been maintained by a local authority or university in the United Kingdom.

Any library the main function of which is to serve the needs of teaching and research at a university in the United Kingdom.

The Historic Buildings and Monuments Commission for England.
The National Trust for Places of Historic Interest or Natural Beauty.
The National Trust for Scotland for Places of Historic Interest or Natural Beauty.
The National Art Collections Fund.
The Trustees of the National Heritage Memorial Fund.
The Friends of the National Libraries.
The Historic Churches Preservation Trust.
Natural England.
Scottish Natural Heritage.
The Natural Resources Body for Wales.
The Marine Management Organisation.
Any local authority.
Any Government department (including the National Debt Commissioners).
Any university or university college in the United Kingdom.
A health service body, within the meaning of section 986 of the Corporation Tax Act 2010.

Note B

GUIDELINES ON THE INTERPRETATION OF PRE-EMINENCE IN RESPECT OF OBJECTS

The following guidelines are intended as a framework of reference for expert advisers to help them in formulating their advice on whether an item is pre-eminent. (An object may fall into more than one category: for example, it may have an especially close association with a particular historic setting and also be pre-eminent, irrespective of this association, under one or more of the other categories).

1. Does the object have an especially close association with our history and national life?

This category includes foreign as well as British works; for example, gifts from foreign sovereigns or governments and objects that have been acquired abroad in circumstances closely associated with our history. It includes objects closely associated with some part of the United Kingdom, or with the development of its institutions and industries. Some objects which fall under this category will be of such national importance that they deserve to enter a national museum or gallery. Others may well be of a lesser degree of national importance, though they will be nonetheless significant in a local context. This category will also include works which derive their significance from a local connection, and which may therefore qualify as pre-eminent addition to a local authority, university or independent museum or gallery.

2. Is the object of especial artistic or art-historical interest?

This category, like 3 below, includes objects deserving of entering a national museum or gallery as well as other objects which may not be pre-eminent in a national museum or gallery, but will be pre-eminent in local authority, university or independent museums or galleries elsewhere, which do not already possess items of similar genre or a similar quality.

3. Is the object of especial importance for the study of some particular form of art, learning or history?

This category includes a wide variety of objects, not restricted to works of art, which are of especial importance for the study of, say, a particular scientific development. The category also includes objects forming part of an historical unity, series or collection either in one place or in the country as a whole. Without a particular object or group of objects, both a unity and a series may be impaired.

4. Does the object have an especially close association with a particular historic setting?

This category will include primary works of art, manuscripts, furniture or other items which have an especially close association with an important historic building. They will be considered pre-eminent by virtue of the specific contribution they make to the understanding of an outstanding historic building. Thus, the category may include paintings, or furniture especially commissioned for a particular house, or a group of paintings having an association with a particular location. They could be associated with a building which is not in the ownership of a Schedule 3 body; closely associated with a historic building that was never completed e.g. Lutyen's plans for Liverpool Metropolitan Cathedral; associated with a building now destroyed e.g. Richmond Palace; objects associated with Cathedrals and historic churches; gardens and landscapes.