CHANGES TO THE UK TAXATION

OF

RESIDENTIAL PROPERTY

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CHANGES TO THE UK TAXATION OF RESIDENTIAL PROPERTY

1. Introduction

The Government announced a package of measures in the March 2012 Budget to ensure that individuals and companies 'pay a fair share of tax on high value residential property' and to tackle avoidance, including the wrapping of property in corporate and other envelopes. The measures included an increase in the rate of stamp duty land tax [SDLT] to 15% for properties costing more than £2m from 21 March 2012 acquired by certain non natural persons [NNPs] including companies, partnerships including a company and collective investment schemes.

HM Treasury subsequently issued a consultation document [condoc] in May 2012 - *Ensuring the fair taxation of residential property transactions* - which focused on two specific parts of the package:

• an annual charge on residential properties valued over £2m owned by NNPs, and

• the extension of capital gains tax (CGT) to the disposal by NNPs of such high value residential property, interests in such property, or the envelopes in which they are held.

The condoc also addressed the need to align the two measures and the 15% SDLT rate as far as possible.

HM Treasury has recently released a summary of responses to the condoc together with their response and draft legislation for inclusion in the 2013 Finance Bill.

2. Summary Of Government's Response

A series of reliefs will be included within the legislation for the ARPT to exclude genuine businesses carrying out genuine commercial activity. These will apply to:

• Property development businesses with dwellings held for the purpose of the property development trade of the company and not occupied at any time by a connected person;

• Property rental businesses with dwellings held for the purpose of letting to third parties for rent on a commercial basis and not occupied at any time by a connected person;

• Property trading businesses with dwellings held for the purpose of a trade of buying and selling property and not occupied at any time by a connected person;

• Properties which are run as businesses with properties open to the public with access to the interior for at least 28 days per year on a commercial basis, as a venue, location or to provide accommodation or other services;

• Dwellings held to provide employee accommodation as long as the employees have less than 5% interest in the company) of the NNP;

• Charities with dwellings held for charitable purposes, unless occupied by a substantial donor to the charity;

• Farmhouses for situations where a working farmer occupies a farmhouse connected to the farm land for the purposes of farming the land;

• Certain other diplomatic, publically owned properties, or property conditionally exempt from inheritance tax.

The 15% SDLT rate legislation will be amended to include a series of reliefs to mirror those in the ARPT legislation, to come into effect from Royal Assent of the 2013 Finance Bill.

These reliefs will also apply for the extended CGT regime, which will apply to disposals of high value UK residential property by non resident NNPs from April 2013. The rate of the CGT charge on these disposals will be 28%, with a tapering relief for gains where the property is worth just over £2m.

As non-resident NNPs are not currently subject to the CGT regime, this charge will apply only to that part of the gain that is accrued on or after 6 April 2013. These changes will come into effect from Royal Assent of the 2013 Finance Bill.

The Government is also considering extending the CGT regime to also apply to disposals of high value residential property by UK NNPs which are currently subject to corporation tax, including on gains they realise on residential property. This would mean that all NNPs, both UK and non-resident, within the scope of ARPT, would be subject to CGT. The Government has asked for views on the impact and implementation of this potential change.

3. Annual Residential Property Tax

From 1 April 2013, ARPT will be introduced for NNPs [companies, partnerships with at least one corporate member and collective investment schemes] holding dwellings valued at over £2 million. The rate of charge is dependent on the value of the dwelling at the 1 April in each year, or the date of acquisition if acquired in a year. The starting rates will be:

Value	Tax
£2m - £5m	£15,000
£5m - £10m	£35,000
£10m - £20m	£70,000
Over £20m	£140,000

These rates will be increased in line with the CPI annually.

The charge will be pro-rated for properties acquired within a charging period, being 1 April to 31 March. The first charge will apply from 1 April 2013 and will be by reference to the property value as at 1 April 2012. The property will need to be re-valued every five years.

The first self assessment return of ARPT for 2013/14 will need to be made by 1 October 2013. Thereafter, returns and payments of ARPT must be made by 30 April annually.

Where a NNP acquires a high value residential property, an ARPT return needs to be submitted within 30 days of the acquisition together with payment of the ARPT.

Different interests in the same dwelling, e.g. freehold reversion and long lease held by the same NNP or by the NNP and persons connected with it will be treated as one whole interest in the dwelling.

There will be reliefs from the charge in relation to property held by certain genuine property businesses, including rental, development and trading businesses as well as property trades deriving income from making a significant part of the property available to the public for at least 28 days a year, non property businesses that make a property available for occupation by employees or partners with less than 5% ownership of the NNP, and farmhouses held by and for the purposes of a farming trade.

The reliefs for rental, development and trading businesses will not be available where the property is occupied by an individual connected with the beneficial owner or by the settlor of a trust where the trustee is connected with the NNP carrying on the business as well as relatives of those individuals.

An NNP must make a nil charge return to claim relief from ARPT.

4. Capital Gains Tax Changes

Whilst draft legislation on the proposed extension of CGT will not be available until January 2013, the summary of responses to the condoc included the following measures:

- A CGT charge will be imposed on non-resident NNPs on disposals on or after 6 April 2013.
- The CGT tax rate will be 28% with tapering relief for gains where the property is worth just over £2 million, which will tax on the lower of the actual gain or the excess of the amount of the disposal value over £2m multiplied by 5/3,
- There will be rebasing to permit the tax charge to apply only to that part of the gain that accrued on or after 6 April 2013,
- Non-UK resident trusts and individuals should not be chargeable on the disposal of their interest in the property,
- As with ARPT, CGT will not apply to genuine property businesses, charities and businesses disposing of employee accommodation,
- Avoidance of CGT by selling a property in a number of separate transactions or by suppressing the total consideration received is likely to be countered by widening existing anti fragmentation rules,
- Losses on the disposal of high value residential property will only be able offsettable against gains on the disposal of high value residential property,
- Where a property is purchased for more than £2m and sold for less than £2m, relief for losses will be limited by treating the disposal proceeds as £2 million,
- Principal private residence relief and indexation allowance will not be available to reduce any capital gain taxed on a NNP subject to the extension of CGT.

The Government has indicated that it is considering extending the CGT regime to apply to disposals of high value residential property by UK resident NNPs, which are currently subject to corporation tax on such gains. The Government has requested views on this by January 2013.

It is noted that the new CGT charge appears only to apply to gains arising on the disposal of direct interests in residential property held by non-resident NNPs. Therefore, if shares in a non resident property company are sold instead, such a disposal should fall outside the scope of the new CGT charge.

The above summary has been compiled from the recently released summary of responses to the condoc and may be subject to change when the 2013 Finance Bill is issued and passes through Parliament.

Proposed high value residential property acquisitions and existing property structures should be reviewed now and any restructuring implemented before April 2013. In all cases specific advice should be obtained before any transactions or changes are contemplated.

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