TURCAN CONNELL

Briefing Note

High Value Residential Properties – the new taxes

In its drive to tackle tax avoidance the Government is introducing three new measures designed to discourage the use of companies and other corporate vehicles to hold high value residential properties, a practice which is referred to as "enveloping". From 21st March 2012 the rate of stamp duty land tax (SDLT) on the purchase of a residential property for more than £2m increased to 15% if the purchaser is a company or other "non-natural" person. In addition from April 2013, a new annual charge will apply to properties worth more than £2m owned by non natural persons; and capital gains tax will be extended to sales of residential properties for more than £2m by (resident and non-resident) non natural persons.

The original proposals have changed in some important respects as a result of consultation, and the number of high value properties likely to be affected has significantly reduced. However for those which are still caught by the new rules, time is short to carry out any restructuring that may be required.

Stamp Duty Land Tax – The 15% Rate

The practice of holding high value residential properties in companies and other corporate vehicles is seen as unacceptable tax avoidance. In order to discourage this practice, a new SDLT rate of 15% applies to acquisitions of residential property for consideration in excess of £2m by certain "non natural persons" from 21st March 2012.

Single Dwellings

The 15% rate applies to "single dwellings", i.e.

- a building which is used, or suitable for use as a dwelling
- a building which is in the process of being constructed or adapted for use as a dwelling.

Where there is mixed use of the property the 15% rate will apply to the part that is a dwelling, if it is valued at more than £2m. Some types of residential accommodation are excluded from the new charge, such as residential accommodation for school pupils and the armed forces, residential homes, boarding schools, halls of residence for students, old people's homes, hospitals, prisons, and hotels.

Non Natural Persons

The 15% rate applies if the purchaser is a “non natural” person, i.e. a company, a partnership with one or more corporate partners or a collective investment scheme. In the case of joint purchasers, if any one of the purchasers is a non natural person, the new rate will apply.

Trusts are not included in the definition of non natural persons and there is a specific exception for corporate trustees (that is, companies acting as trustees of settlements). Bare trustees are disregarded and the 15% rate will apply if the underlying beneficial owner is a “non natural person”.

Charities are not subject to the increased rate, and the general exemption from SDLT for acquisitions by charitable bodies continues to apply.

Proposed New Reliefs

As currently enacted, the legislation relieves property development businesses from the 15% rate. The relief as it currently stands is rather restrictive and applies only where the business consists of or includes buying residential property and redeveloping it for resale. In addition, the company must have carried on the business for at least two years before the transaction.

The reliefs from the charge are to be significantly extended, but only from the date on which the Finance Act 2013 receives Royal Assent (likely to be July 2013). This leaves a period of around 16 months (March 2012 – July 2013) in which only the rather restrictive relief for property development business applies. Under the proposed new reliefs, the 15% rate will not apply to properties used in any of the following activities:

- property rental businesses
- property development trades
- exchanges in the course of a property development business
- sales in the course of a property trading business
- a trade carried on on a commercial basis with a view to profit which involves making the property open to the public, or available to the public to stay in or otherwise use
- properties acquired as accommodation for employees employed in a trade that is not a property rental, property development, or property trading business
- farmhouses occupied for the purposes of a farming trade by a farm worker who has substantial day to day involvement in the farming trade

These reliefs can be withdrawn if, within three years of the relief being granted, the property ceases to be used for a relievable purpose, or (in the case of a property rental business, a property development business or a property trading business) an individual connected with the owner uses the building.

Annual Residential Property Tax

From 1st April 2013 a new tax known as the annual residential property tax (ARPT) will apply to residential properties valued at over £2m owned by certain types of non natural persons. The stated aim of the annual charge is "to deter avoidance and to ensure the owners of high value residential property pay their fair share of tax." The intention is that the charge will encourage anyone who has enveloped a high value residential property to take it out of its envelope thereby ensuring that SDLT will be payable on any onward sale of the property.

Non Natural Persons

The new charge will apply to "non natural persons" and the definition of non natural persons will be the same as for the SDLT 15% rate namely companies, partnerships of which one of the partners is a company and collective investment schemes. Properties that are jointly owned will be subject to the annual charge if one or more of the joint owners is a non natural person. Charities and trustees (other than bare trustees) will be excluded from the charge.

Reliefs

The same reliefs will apply to ARPT as for the 15% SDLT charge and further reliefs are to be introduced for charities, public bodies, properties used for diplomatic purposes and properties conditionally exempt from inheritance tax.

Single Dwellings

ARPT will apply to "single dwellings" which is defined in the same way as for the 15% SDLT rate. In the case of mixed use property, the charge will apply only to the residential part. Residential properties such as boarding schools, hospitals, student halls of residence, military accommodation, care homes and prisons are to be exempted from the change.

Valuation

The new charge will be calculated on the basis of a market valuation of the property concerned at the relevant valuation date, and that value will apply for the next 5 years. The valuation date for properties which are subject to the new charge from 1st April 2013 is the value of the property on 1st April 2012 if the interest was owned on that date, or the value at acquisition if it is acquired after that date.

Properties are to be revalued every five years.

Rates Of ARPT

The proposed bandings are as follows:

Property Value	**ARPT 2012-13**
£2m - £5m	£15,000
£5m - £10m	£35,000
£10m - £20m	£70,000
£20m +	£140,000

The annual charge will be indexed to the consumer price index and uprated in April each year based on the CPI of the previous September. This will commence from the second year of charge, 1st April 2014.

Property owners will have to submit an annual charge return to HMRC for each property subject to the new charge. The intention is that HMRC and the Valuation Office Agency will offer a pre return valuation checking service. Property owners will be able to submit their proposed valuations to HMRC for checking and where a proposed banding cannot be accepted, the Valuation Office Agency will attempt to agree the matter with the taxpayer.

HMRC will be responsible for administering the new annual charge. Penalties will be payable for failure to make a return and submitting initial valuations that are low because of negligence.

Capital Gains Tax on Residential Properties worth over £2m

From 6th April 2013 non natural persons, both UK resident and non resident, will be subject to capital gains tax on disposals of UK residential properties for more than £2m, if the property is within the ARPT regime. The rate of capital gains tax will be 28% with a tapering relief for gains where the property is worth just over £2m. An important change to the original proposal is that the capital gains tax charge will apply only to the part of the gain that is attributable to the period on or after 6th April 2013, effectively rebasing the property to 5th April 2013 for the purposes of this CGT charge only. The pre 6th April 2013 gain may remain taxable under other provisions.

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Under the government's original proposal the scope of the new CGT charge would have been significantly wider than the ARPT and would, for example, have included trusts. In response to concerns expressed in the consultation process, it has now been decided to align the CGT charge with ARPT, and it will therefore apply only to entities within the ARPT charge, namely companies, partnerships with one or more corporate partners, and collective investment vehicles.

The new charge will apply where a non natural person disposes of a residential property for a consideration in excess of £2m, and there will be provisions to prevent fragmentation of property transactions to avoid breaching the threshold. The government has withdrawn its original proposal to apply the extended CGT regime to disposals of interests in companies and collective investment arrangements which own high value residential properties in the UK.

The ARPT definition of dwelling will be adopted for the purposes of the new CGT charge. Losses on disposals of high value residential properties will be available to offset only against gains on disposals of other such property. Losses will only be allowed down to the £2m threshold.

This note is intended as a brief summary of the new taxes regarding high value residential properties as at March 2013. Taxation is subject to change and depends on the individual circumstances of each client. Legislation is also subject to change. No responsibility can be accepted for any action taken in reliance of this note and specialist advice should be taken in every case. Turcan Connell would be happy to provide such advice. Should you require further advice please contact either Heather Thompson at heather.thompson@turcanconnell.com or Donald Simpson at donald.simpson@turcanconnell.com