

UK tax considerations on investments in UK property

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Introduction

UK real estate, and especially prime property in London, has always attracted significant international investment as it provides excellent returns and protection of capital. This Information Sheet addresses, in an outline, the main UK tax considerations when investing in UK property.

Main reasons to invest in UK property

- Favourable place to invest
- The market is very liquid
- Availability of mortgage finance
- One of the world's major financial centres
- Generate capital gains on eventual sale
- Potential rental income generated throughout the period of ownership

Net returns on capital and income depend on a host of factors, including tax.

Initial UK tax considerations

- There are various taxes applicable on acquisition, during ownership and upon disposal of UK properties.
- Some of these taxes may be mitigated through proper planning.
- Essentially, a number of structures may be suitable depending on the use and type of the particular property (e.g. residential or commercial property) and investor circumstances / intentions.

1. UPON ACQUISITION: Main UK taxes
1.1. VAT - Standard rate 20%

- The acquisition of UK property and the cost of ancillary services (e.g. legal, architects and survey fees, estate agents charges) may be subject to UK VAT which is payable by the purchaser (currently at 20%).
- **Commercial Property:** The acquisition of UK commercial property is generally subject to the UK standard rate of VAT (20%). The VAT charge however may be eliminated through proper planning.
- **Residential Property:** The acquisition and letting of residential properties generally falls outside the scope of VAT.

1.2. Stamp Duty Land Tax ('SDLT')

Stamp Duty Land Tax ('SDLT') is payable by the purchaser when buying a property in the UK over a certain price. The SDLT rate depends on:

- the purchase price of the property
- whether the property is residential, commercial, or mixed use
- whether the buyer is a non-natural person (e.g. a company)
- whether the sale contract for non-residential transactions has been exchanged before or after 17 March 2016

Residential transactions with effective date on or after 4 December 2014 (slice system)		Non-residential or mixed (slab system) before 17 March 2016		Non-residential or mixed (slab system) after 17 March 2016	
Consideration	Rate	Consideration	Rate	Rate	Rate
Not more than £125.000	0%	Not more than £150.000	0%	Not more than £150.000	0%
More than £125.000 but not more than £250.000	2%	More than £150.000 but not more than £250.000	1%	More than £150.000 but not more than £250.000	2%
More than £250.000 but not more than £925.000	5%	More than £250.000 but not more than £500.000	3%	More than £250.000	5%
More than £925.000 but not more than £1.5 million	10%	More than £500.000	4%		
More than £1.5 million	12%				
Where the purchaser is a "non-natural person" (e.g. company) and effective date is on or after: <ul style="list-style-type: none"> • 21 March 2012 and the chargeable consideration is over £2 million • 20 March 2014 and the chargeable consideration is over £500.000 					
	15%				

2. DURING OWNERSHIP: Main UK taxes

2.1. Annual Tax on Enveloped Dwellings ('ATED')

The ATED is applicable as from 1 April 2013 and is paid annually by **non-natural persons** (e.g. companies, partnerships) that own high value residential property situated in the UK. ATED is the new term for what was previously known as the "annual residential property tax".

The ATED rates from 1 April 2016 to 31 March 2017 are as follows:

Property value	Annual charge
More than £500,000 but not more than £1 million	£3,500
More than £1 million but not more than £2 million	£7,000
More than £2 million but not more than £5 million	£23,350
More than £5 million but not more than £10 million	£54,450
More than £10 million but not more than £20 million	£109,050
More than £20 million	£218,200

Compliance: If the property falls within the scope of ATED, then regardless of any reliefs that may apply, a return must be sent to HMRC. Failure to comply with this reporting and payment will result in penalties and interest.

Reliefs: The law provides for certain reliefs from ATED. Main reliefs are given in case of properties which are rented out, or the property is under development with a view to dispose it. In addition, Trustees (including corporate trustees) are not subject to the ATED where they hold property directly.

There is significant scope to eliminate this tax through proper planning.

2.2. Tax on rental income

UK income tax is charged on income from renting property situated in the UK irrespective of the residence status of the landlord.

Companies: In general, UK companies are taxed at 20% on their net rental income. Non-UK resident companies having UK property for investment purposes are also taxed at the rate of 20%. UK legislation generally allows for the deduction of interest on debt used to finance the acquisition of the property. Connected party relief is restricted to the amount of interest payable on the open market. Other expenses directly related to the rental activity (such as maintenance, repairs etc.) may also be tax deductible. Capital expenditure (i.e. repair works) is not deductible from rental income but is instead taken into consideration when calculating any gain arising on a disposal of the property (provided such repairs enhance the property's value).

Individuals: The rental income net of deductible expenses is subject to UK tax in the hands of the individual in accordance with the UK income tax band rates which vary from 20% to 45%. Many non-resident individuals (Commonwealth or EEA citizens) may claim a personal tax-free allowance of £11,000 (for 2016/2017). The top rate of 45% applies to incomes in excess of £150,000.

Trustees: An offshore trust would be subject to UK tax on the net rental income at the rate of 20% or at the rate of 45% (with certain allowances). The applicable rate depends, amongst other factors, as to whether the trust is considered as a discretionary trust or not.

3. UPON DISPOSAL / SUCCESSION: Main UK taxes

3.1. Capital Gains Tax ('CGT')

The UK government has confirmed that, from 6 April 2015, non-UK resident persons (including individuals, trustees, personal representatives and certain closely-held companies), will be subject to capital gains tax on disposals of UK residential property. The rates for 2016 / 2017 are:

- **Non-resident individuals** will be subject to tax at the same rates as UK resident individuals (18% or 28% depending on the total amount of taxable income)
- **Non-resident companies** will be subject to tax at the same rates as UK companies (20%) and will have access to an indexation allowance
- **Trustees or personal representatives of deceased persons** will be subject to tax at the rate of 20% for non-residential property and 28% for residential property

Note: The capital gain is basically calculated by deducting the **value of the property as at 5 April 2015** (or subsequent date of acquisition cost) from the sales proceeds, plus any necessary adjustments.

Note: The CGT should not apply on a potential disposal of the shares of a non-UK resident entity owning any underlying UK property.

3.2. Inheritance Tax ('IHT')

Companies: The shares of a non-UK company are considered a non-UK asset, thus are not subject to UK IHT. This may not apply to persons holding the shares of a non-UK company where they are considered domiciled or deemed to be domiciled in the UK.

Individuals: IHT at 40% is payable with respect to UK situated property on the death of an individual owner (and certain other gifts and lifetime transfers which incur a 20% IHT rate) regardless of his residence or domicile status. In the case of a non-UK resident who has had no prior connection with the UK, only UK located assets will be within its scope.

The tax is calculated by reference to the net value of the property (less any debt or other allowances) over and above the 'nil-band' rate which currently is £325,000. Many transfers are "potentially exempt" from IHT and only create a charge to tax where death ensues within 7 years of the date of the transfer.

Trustees who hold UK property are subject to a 10-year IHT periodic charge at a maximum rate of 6% on the value of the property, although the charge is only assessed on the value of the property less any debt. In certain cases (as in the case of a non-discretionary trust), where beneficiary is succeeded, the trustees could also be subject to the 40% IHT described above.

Concluding remarks

- Irrespective of the fact that the owners of the property may be non-UK tax residents, they will still be faced with UK tax issues throughout the lifecycle of the property (acquisition, ownership, disposal), on account of the fact that the property is situated in the UK and any relevant income is sourced in the UK.
- Notwithstanding the above, non-UK resident owners of UK property may also be faced with potential tax issues in their own home jurisdiction, as a result of holding and/or disposing of a foreign property. Such issues should be examined separately.

NOTES

The above is intended to provide a brief guide only. It is essential that appropriate professional advice is obtained. Totalserve Management Ltd will be glad to assist you in this respect. Please do not hesitate to contact us.