UK200Group
tax
talking tax

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All change for property companies

The concept of a 'mansion tax' on high value property was trailed in advance of the 2012 Budget as a Lib Dem bargaining chip in exchange for scrapping the 50% income tax rate. Whilst the political machinations that resulted in the Budget are inevitably opaque, what is clear is that neither coalition partner got exactly what they wanted.

The primary focus of the three measures announced in Budget 2012 is a crack down on SDLT avoidance in relation to high value residential property. Consultation is now taking place on two of the three measures, but not on the SDLT changes which take effect from 21 March 2012. SDLT avoidance and evasion is estimated to cost the government £200m per year and the government's particular concern is the 'enveloping' of high value property within a company. There was, of course, no saving on the way into the company, but the shares could be transferred on with a 0.5% stamp duty cost rather than the 5% SDLT. With that in mind, two new rates of SDLT have been introduced: a 7% rate for residential property transfers at more than £2m and a 15% rate where such properties are purchased by a 'non-natural person' - effectively any structure involving a company or similar.

Although the SDLT charge at 15% covers the tax due on an identical transaction between two individuals twice over, it takes no account of any growth in value of the property between transfers. So, to further discourage enveloping, an additional Budget measure introduces an annual charge on interests in high value residential property owned by non-natural persons. As proposed, the charge will apply to enveloped properties from 2013/14 onwards if the property is valued at more than £2m. Annual charge rates start at £15,000 for properties in the £2-5m band and go up to £140k for those valued at over £20m.

The consultation document has started to flesh out more details on how the charge will work. The valuation date for property structures already in place is 5 April 2012 and, as a revaluation exercise will only be required every five years, it should be possible to rely on the April 2012 valuation until 2017/18. The charge itself will be indexed by updating each April for the CPI. There is, however, no mention of indexation of the thresholds, so unless there is a period of extended stagnation in the UK property market, an element of fiscal drag seems to be being built into the structure. One wonders how long it will be before the annual charge is being applied to a suburban semi.

We are told that penalties will apply where the property in question is undervalued for annual charge purposes unless the non-natural person has taken proper care to establish a correct value, generally by hiring a suitably qualified valuer to provide an opinion. A pre-return valuation check is to be offered by the VOA, but it is not clear whether this will be available to those whose property is valued in the region of but possibly less than £2m.

Property investors currently have no exemption; neither do developers until they have been operating for two years. The single purpose company, often used for developments in short-term joint venture situations, would therefore appear to be caught.

Many of the people affected by the Budget proposals will be non-resident, non-domiciled investors, for whom an offshore company is an appropriate holding structure for ensuring that there is no exposure to UK inheritance tax on the property value. For them, the third measure, extension of capital gains tax to £2m+ residential property owned by non-resident non-natural persons will be particularly unwelcome. Given that, like the annual charge, the CGT extension does not take effect until April 2013, there is an opportunity to de-envelope in the next eight months. This is certainly what the government would like property owners to do. Offshore holders of £2m+ properties therefore face a choice between retaining the IHT advantages of a company structure or the additional tax and professional costs which will result from the new regime.

The exact operation of the annual charge and capital gains extension will only really be clear after the results of the consultation are published. In the meantime while various Budget 2012 proposals have been reversed, there is every sign that these new measures will go ahead and owners of property companies need to do some thinking between now and April 2013.

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Clare is also presenting a session on 'Tax structures for UK Property holdings' at our Property & Construction Training course taking place in London on the 25 September 2012

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