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UK residential property owned by non-UK residents

The UK's stable political environment and track record of good returns on investment in residential property has attracted large numbers of overseas buyers for many years. Some use the property as a base for family visits to the UK, but others are simply investors looking for a safe haven for their money, good returns and prospects for capital growth. The prime London residential market has certainly not disappointed in recent years – good returns were produced throughout the financial crisis which hit in 2008 and, as the UK leads the way out of the global recession, rents and capital values have soared.

However, existing owners and prospective buyers based overseas need to be aware of the recent tax changes which impose obligations on them to take action, and which may significantly affect their returns and longer-term strategy.

The UK as a tax haven?

Non-UK residents did not usually have to worry about UK capital gains tax (CGT), and non-UK domiciliaries could easily avoid inheritance tax by holding the property through a non-UK company. Use of an overseas company also meant that on sale of the company rather than the property only 0.5% stamp duty was payable on shares rather than the rates of stamp duty land tax – then up to 5% - applicable to residential property, increasing the attractiveness of the property to some buyers.

Much of this has now changed.

Annual tax on enveloped dwellings (ATED)

Since April 2013 'high value' UK residential properties owned by 'non-natural persons', if occupied by someone connected with the owner, have been subject to ATED. Non-natural persons for this purpose are companies, partnerships with a corporate member and other collective investment vehicles, including offshore companies. ATED is an annual tax charge based on the value of the property on 1 April 2012, or the cost at acquisition if later. Initially it applied to 'dwellings' worth over £2 million, but this threshold fell to £1 million from 6 April 2015 and falls to £500,000 from 6 April 2016.

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The annual ATED liability is:

Property value	2013/14 £	2014/15 £	2015/16 £	2016/17 £
£500k - £1m				3,500
£1m - £2m			7,000	TBA
>£2m - £5m	15,000	15,400	23,350	TBA
>£5m - £10m	35,000	35,900	54,450	TBA
>£10m - £20m	70,000	71,850	109,050	TBA
>£20m	140,000	143,750	218,200	TBA

Non-natural persons with high value properties have to file a return each year. This must include any claim to an exemption, so even those with no tax to pay must file the return. Any tax due must be paid within 30 days of the liability arising.

ATED-related capital gains

When the ATED charge is payable on a property, any gain on its disposal which is attributable to the ATED period of ownership is liable to 28% CGT.

Non-residents' capital gains tax

New provisions have applied since 5 April 2015 to gains on UK residential property realised by non-resident individuals (on their own or in partnership), non-resident trustees, personal representatives of a non-resident deceased person and non-resident companies controlled by five or fewer persons (except where that company or at least one of the controlling persons is a 'qualifying institutional investor'). ATED-related gains are excluded from this new charge.

Affected property

The new rules apply to gains realised on the disposal of UK residential property and property which has the potential to be used as a residence. This includes property which is currently being built or adapted for residential use.

Residential property used on a communal basis such as care homes, school boarding houses, military accommodation, hospitals, hospices, prisons and purpose-built student accommodation with at least 15 bedrooms is exempt from the new charge.

Calculation of gains

Only the increase in value after 5 April 2015 is subject to the new tax charge. For properties held then a valuation at that date will therefore be required. Alternatively, those affected can elect for the gain to be calculated by time apportionment since acquisition, charging only the proportion of the gain attributed to the period after 5 April 2015.

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Rate of tax and payment

For individuals, the CGT charge will be 18% for basic-rate taxpayers and 28% for higher-rate taxpayers. The applicable rate will be determined by the non-resident's UK income for the year. Non-resident trusts will be liable at 28% and the rate for companies is 20%. The normal annual CGT exemptions will apply to individuals and trustees.

Almost all disposals have to be reported within 30 days of completion and the tax paid at the same time, unless a UK tax return is already filed normally. This is a challenging timetable, given that most non-UK residents will not have UK tax reference numbers.

Exemptions

The charge applies not only to owner-occupied properties but also to those let out – in contrast to the ATED rules where properties let to third parties are exempt if the appropriate claim is made in the annual return. The CGT main residence exemption can only be claimed in relation to a UK home by a non-UK resident owner who has spent at least 90 days in their UK home(s) in that tax year.

Stamp Duty Land Tax

The rates of Stamp Duty Land Tax (SDLT) on residential property have soared in recent years, so that the normal rate on purchase consideration in excess of £1.5m is 12%. Furthermore, a 15% rate applies to purchases by non-natural persons where the consideration exceeds £500,000, save for those properties where similar exemptions apply as with ATED (developers, let to third parties, etc.).

Inheritance tax

Currently, UK residential property is often held within an offshore company by those not domiciled in the UK, to avoid UK inheritance tax. The government proposes that, from 6 April 2017 the value of shares in 'closely-held' offshore companies attributable to UK residential property will be subject to inheritance tax. The proposals are subject to consultation on the detail.

Finance costs

Currently interest payable on amounts borrowed to buy or improve land and buildings held as an investment is deductible from rents for income tax purposes. From 6 April 2017 a restriction on the tax relief for finance costs of individuals and trustees letting residential property is to be phased in so that from 6 April 2020 only basic rate (20% relief) is allowed.

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Action required

Those owners who are caught by the ATED must file their special returns and pay the ATED tax.

They may also wish to review whether the current ownership structure remains the best.

Non-residents will need to take account of the new CGT rules which apply to UK residential property when evaluating investment opportunities. Existing owners may wish to obtain a formal valuation as at 5 April 2015 so that they can choose the most beneficial method of calculating the gain on a future disposal.

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