



BARNES ROFFE LLP

**PROPERTY AND TAX
PLANNING**

13 SEPTEMBER 2018



BARNES ROFFE LLP

STEPHEN CORNER

FCA, LLB (Hons), Barrister

Partner



THE LANDSCAPE

Tax avoidance has become immoral

There is an estimated £5B tax gap in the rental sector

SDLT Rates are creating structural issues in the property market

Brexit is creating uncertainty/interest rates rising

HMRC interest restrictions are now biting

There is a shortage of low cost housing

Making Tax Digital (MTD) is on the way



TAX RATES

Capital Gains Tax Rate
Residential Dwellings

18% within basic rate band
28% otherwise

Corporation Tax rate 19%

Inheritance Tax 40%



RELIEF ON DISPOSAL OF PRIVATE RESIDENCES

CGT exemption for only or main residence

Permitted area of 0.5 of a hectare

Area can be increased having regard to the size and character of the dwelling house



PPR

Where there is more than one residence, can elect within 2 years which has the exemption

Once election is made it can be amended

Husband and wife can only have one main residence



PPR EXEMPTION

Gains are exempt for a period of residence or deemed residence

Get last 18 months in any event

£40,000 letting exemption

Other periods of absence not exceeding 3 years



ISSUES WITH PPR RELIEF

The property must have the quality of a residence

Capable of proper occupation

Sufficient degree of permanence/intention

Part of the dwelling used exclusively for business

Exclusion of relief for a gain attributable to
expenditure incurred with the intent of realising a gain



RENT A ROOM RELIEF

£7,500 p.a.

Resident landlord (whether owned or not)

Includes a bed & breakfast guest house

Does not include homes converted into separate flats



BUILDING ON YOUR PPR PLOT

If you demolish to rebuild there is a deemed disposal at the market value of the plot





PPR & IHT PLANNING

Risks associated with IHT planning for PPR

Gifts with reservation of benefit
(rental / occupation)





NOW A LOOK AT...

PROPERTY INVESTMENT

PROPERTY RENTAL BUSINESSES



WEAR AND TEAR ALLOWANCE

Abolished April 2016

Instead cost of replacement domestic items is deductible
e.g. moveable furniture, TVs, white goods, floor coverings,
curtains, linen, crockery and cutlery

Applies to furnished and unfurnished accommodation

Applies to corporates and individuals

Replacement of fixtures is allowable as repair



CAPITAL ALLOWANCES AND RENTED PROPERTIES

Capital allowances are available on commercial properties
(see below)

For residential properties, no CAs are available on white goods or integral features (boilers, heating, electrics, etc)

CAs are available for “plant” used for property maintenance and management – e.g. cars and vans

Different rules for furnished holiday lettings



CAPITAL ALLOWANCES AND COMMERCIAL PROPERTY

Capital allowances are available for the “plant” effectively built into a commercial building – includes everything from an industrial shed to Grade A offices

Includes everything from bathrooms, heating to air conditioning and lifts, etc

Can be around 35% of the build costs of Grade A office space



CAPITAL ALLOWANCES AND COMMERCIAL PROPERTY

Where a new build look to actual costs

Where acquiring a second-hand building can only claim where (generally) the vendor has claimed CAs - you take on the vendor's pool of unused allowances – but there is an election for another value (less than or equal to cost)

Claiming capital allowances does not reduce the CGT base cost
(double tax allowance)



INCREASED RATES OF SDLT ON DWELLINGS

BAND	STANDARD RATE	ADJUSTED RATE
Up to £125,000	0%	3%
£125,001 - £250,000	2%	5%
£250,001 - £925,000	5%	8%
£925,001 - £1,500,000	10%	13%
Over £1,500,001	12%	15%

Applies to second properties and all corporate purchases.
Does not apply to land, mixed use property or more than six properties purchased in a single transaction



RESTRICTION OF INTEREST RELIEF

Applies to borrowings on UK and foreign properties from April 2017

Does not apply to:

Furnished holiday lets

Property businesses subject to Corporation Tax

Commercial property



GRADUAL RESTRICTION OF HIGHER RATE TAX RELIEF

TAX YEAR	DEDUCTION FOR BASIC RATE TAXATION	DEDUCTION FOR HIGHER RATE TAXATION
2017-2018	100%	75%
2018-2019	100%	50%
2019-2020	100%	25%
2020-2021	100%	0%



HOW DOES THE RESTRICTION ACTUALLY WORK?

EXAMPLE:

Mr Greenacre has other income equal to his basic rate tax band and personal allowance

He has property income before finance costs of £20,000 and finance costs of £20,000

His tax liabilities will be as follows:



HOW DOES THE RESTRICTION ACTUALLY WORK?

EXAMPLE cont/. . .

Mr Greenacres's tax liabilities

TAX YEAR	DEDUCTION FOR HIGHER RATE TAXATION	TAXATION PAYABLE
2017-2018	75%	£1,000
2018-2019	50%	£2,000
2019-2020	25%	£3,000
2020+	0%	£4,000

Basic rate taxpayers will become higher rate taxpayers!



OTHER POTENTIAL EFFECTS OF THE RULE CHANGE

Interest is no longer a deduction from income!

Increased “income” may increase student loan repayments

Income over £50,000 creates child benefit clawback

Lose personal allowances once income exceeds
£100,000



WHAT CAN YOU DO TO REDUCE TAXABLE PROFITS?

- Use of home as office
- Capital allowances on office equipment
- Travel costs to property
- Postage and stationery costs
- Phone costs
- Commercial salaries for family members



WHAT ABOUT . . .

**INCORPORATION
OF A
PROPERTY BUSINESS?**



ADVANTAGES OF INCORPORATION

Companies are not affected by the restriction on finance costs

Income surpluses can be retained within the company at 19% - facilitating faster amortisation of debt

Properties are re-based to market value on incorporation



DISADVANTAGES OF INCORPORATION

Additional costs of running a company

Income tax payable on income extracted from the
company

Costs of incorporation



IS INCORPORATION EASY?

What are the obstacles?

- Capital Gains Tax
- SDLT
- Re-financing of mortgages (often attractive fixed rates!)



OBSTACLES TO INCORPORATION CAPITAL GAINS TAX

Where property rental activities amount to a “business”, it is possible to hold over any gains arising on incorporation into shares issued by the acquiring company on incorporation

The relief requires that all properties that are part of the business are incorporated at the same time into the same company

This means that commercial and residential properties in the UK and abroad will usually be regarded as a single business activity

Private or family use (not rented) properties will generally be excluded as they are not business assets



OBSTACLES TO INCORPORATION CAPITAL GAINS TAX

What is the distinction between property investment and a property rental business?

There are a number of features of a business set out in the case law including:

- Substance, earnest pursuit, business like approach
- Does it matter how much time is spent in the business by the owner?



OBSTACLES TO INCORPORATION SDLT

You must have a **Partnership** to claim exemption from SDLT on incorporation

Partnerships do not arise from simple “joint ownership” of property



OBSTACLES TO INCORPORATION SDLT

Types of Partnerships

**What if you are starting off with no
Partnership?**



DO YOU HAVE TO . . .

RE-FINANCE ON INCORPORATION?

NO . . . BUT . . .





PROPERTIES IN COMPANIES - ATED

Applies to dwellings held in part by non-humans

Must file a return each year by 30 April to avoid heavy penalties

Exemptions apply where there is business and no “personal connected” use



ATED RATES

FROM	UP TO	CHARGE
£500,000	£1,000,000	£3,500
£1,000,001	£2,000,000	£7,050
£2,000,001	£5,000,000	£23,550
£5,000,001	£10,000,000	£54,950
£10,000,001	£20,000,000	£110,100
£20,000,001		£220,350



ATED

Rates of CGT for ATED COMPANIES – 28%





RESIDENTIAL PROPERTY HELD BY NON-RESIDENTS

CGT charge on post 5 April 2015 gains on UK residential property

Properties are revalued on 5 April 2015

Return of the gain and tax payable 30 days post completion!

(applies to commercial property from 6 April 2019)



WHAT IF YOU ARE A TRADER?

A trade is “every trade, manufacture, adventure or concern in the nature of a trade”

Stand back and look at the whole picture

Marsden v. Morton



TRADING

If trading in own name, profits are subject to
Income Tax and National Insurance (47%)

Therefore most trading is undertaken in
companies (19% Corporation Tax)



ENTREPRENEURS' RELIEF

10% CGT rate on the sale and capital distributions from a trading company (including a property trader) after a 12 month qualifying period

Led to SPVs being liquidated after a single deal to get an overall rate of 27.1%

New anti-avoidance rule where a similar activity is undertaken within a 2 year period



BUSINESS PROPERTY RELIEF (IHT)

A 100% exemption for IHT with very limited applicability to property or property company shares

Applies only to shares in property development companies / developments

Issues once developments are completed



IHT - BPR

After a two years' qualifying period, BPR applies to shares in trading companies (not property trading companies)

Company has to be “wholly or mainly” a trading company or holding company of a trading group

Issues with property investments in trading companies - solution may be a demerger



REASONS TO DEMERGE PROPERTY INVESTMENTS

BPR – 50%

ER – 20%

Issues with s.165 gift relief for shares



IHT – AGRICULTURAL PROPERTY RELIEF

Covers agricultural land, pasture, woodland, farm buildings, farm cottages & curtilage, farm houses, stud farms, land in habitat schemes

Relief applies to farm cottages and houses of appropriate character

Applies to agricultural value only



IHT - APR

Occupied by self for agricultural purposes for 2 years before the event

or

Owned as an investor for 7 years and occupied by someone else for agricultural purposes

Applies to shares in farming companies



USING LLPs

What if a company has the deposit to buy a property but it is wished to buy the property personally?

Consider forming an LLP with the company as a member so that the company's equity can fund the purchase without s.455, etc

Rent will be used to fund the loan and income will largely accrue to the company

Any gains can accrue to the individual owners that have contributed minimal equity



PROPERTY AND PENSION SCHEMES

Growth and income is exempt

Contributions (within allowed limits) are tax deductible

Cannot hold residential property

Profits from LLP interests are taxable!

Pension liberation make pensions more flexible



PROPERTY AND VAT

Generally, VAT is limited to commercial properties in respect of which there has been an option to tax – on new builds there is always VAT

Issues with purchasing commercial property where the vendor has opted to tax

The concept of a TOGC

Note where VAT is charged, SDLT is charged on the VAT inclusive amount!

Why would you opt to tax for VAT?



VAT – RESIDENTIAL NEW BUILDS

The first supply of a new build residential property is a zero rated supply allowing full recovery of VAT – issues where the first supply is a rental as perhaps the market is bad!

No recovery of VAT on white goods, etc

Builder will zero rate new build contracts



CONVERSION TO RESIDENTIAL

There is a reduced rate of VAT charged on the building contract of 5%

Applies where the building was previously residential and there is a change in the number of residential units

Also applies where a property has been empty for two years and the work is commercial within 12 months of acquisition



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