Taxing times

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Robert Walker sets out changes to the taxation of non-residents? UK property gains

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In the autumn budget , the government announced a major change in the taxation of UK immovable property for non-resident investors. From April 2019, UK tax will be charged on gains made by non-residents on direct disposals of such property in the UK, and on some indirect disposals.

This was far from expected, and the proposal significantly extends the existing non-resident capital gains tax (NRCGT) and annual tax on enveloped dwellings (ATED)-related gains regimes, which apply to direct disposals of residential property.

Unlike most other major jurisdictions, the UK has not to date taxed non-residents disposing of non-residential UK real estate. It also has not taxed widely held, non-resident companies on disposals of interests in UK residential land, or on indirect disposals of such land, as for example when companies that own UK land are sold by non-residents.

The proposals to start taxing non-residents on gains follow other recent changes extending the scope of UK taxation in relation to profits on the direct or indirect disposal of UK immovable property that are trading in nature (see RICS Property Journal December 2016/January 2017, p.18).

In addition, it is proposed that from April 2020, UK property income received by non-resident companies will be chargeable to UK corporation tax, rather than income tax.

Proposals overview

The proposals will apply to both direct and certain indirect disposals of UK real estate by non-UK residents.

Non-resident companies will be subject to corporation tax on their direct and indirect UK real-estate gains; UK capital gains tax will be the rate payable by non-resident investors except companies.

The application of the new rules to direct disposals of UK property by non-resident investors is relatively straightforward. The proposals for indirect disposals, however, require a little explanation.

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the scope of UK taxation in relation to profits

The indirect disposal rules will apply to a disposal of an entity, for example, a company that is property-rich, which is the case where, broadly, 75% or more of its gross asset value at disposal is represented directly or indirectly by UK real estate. Such disposals will trigger the charge only where the person holds, or has held at some point within the five years prior to the disposal, a 25% or greater interest in the entity.

Special provisions will apply to aggregate holdings to prevent fragmentation of interests that bring them below 25%, and also to staggered disposals, including provisions where investors are acting together.

Exemptions

Entities currently exempt from UK tax on capital gains, such as overseas pension schemes, or otherwise outside the scope of UK tax for reasons other than residence should continue to be exempt or out of scope on gains on disposals they make directly.

In addition, the substantial shareholding exemption rules, expanded in 2017, will wholly or partially exempt disposals by companies held by certain qualifying institutional investors, such as registered pension schemes, certain overseas pension schemes, life assurance companies, sovereign immune persons, charities and certain investment trusts.

In the absence of any new provisions, this may mean tax-exempt investors such as UK pensions funds or charities investing in UK real estate through offshore unit trusts may well become liable for UK tax at the unit trust level, where they are making the disposal.

Calculating gain

For non-residential property, and residential property not currently liable for NRCGT- or ATED-related gains charges, only the gains attributable to changes in value from 1 April 2019, for companies, or from 6 April for other persons, will be chargeable.

For direct disposals, this will be achieved by rebasing property values at April 2019, with the option to compute the loss or gain on disposal using the acquisition cost as the base cost of the property.

For indirect disposals, April 2019 is also stated to be the rebasing point. There is no proposal to offer an original cost alternative.

Anti-avoidance

An anti-forestalling rule will apply to certain arrangements entered into on or after the publication of the consultation document on 22 November 2017.

The rule is intended to counteract arrangements that seek to avoid the new charge on non-residents by exploiting provisions in some tax treaties in a way that is contrary to the object and purpose of those provisions, particularly with respect to arrangements designed to frustrate the operation of the charge on indirect disposals. A targeted anti-avoidance rule

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will also apply from April 2019.

Consultation

The government carried out a consultation to seek 'to ensure that the legislation is effectively targeted and does not place unnecessary burdens on affected taxpayers', and this closed to responses in February.

We understand that the principal aspects of the reforms are fixed ? for example, who falls within its scope, the commencement date and the core features of the direct and indirect disposal provisions. However, there will still be consultation on the detailed aspects of the provisions and their unintended consequences.

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Further information

- Related competencies include: Taxation
- This feature was taken from the RICS Property Journal (May/June 2018)
- Related categories include: Capital allowances and Taxation of real estate

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