Trew Tax Services

New Capital Gains Tax Rules for Non-Residents selling UK Residential Property.

OVERVIEW

Prior to 6th April 2015, individuals who were resident outside of the U.K were not subject to Capital Gains Tax on the sale of UK assets.

A change to this legislation took effect on 6th April 2015 specific to sales of residential property. The result of the change means that any sale of UK residential property by a non- resident could be subject to capital gains tax in the UK.

REPORTING REQUIREMENTS

The sale must be reported to HM Revenue and Customs within 30 days of the conveyance. There is an on-line process to follow. This reporting requirement applies whether tax is payable or not.

TAX CHARGE

Tax is calculated on the amount of the gain which accrued post 6th April 2015. This is likely to mean that there will be few due to pay tax in the first year of the new regime but the number will steadily increase over time. There are three ways in which the accrued gain can be calculated.

Default Method

The property must be valued at 6th April 2015 and the chargeable gain calculated on the difference between that figure and the proceeds received.

Straight Line Apportionment

The chargeable proportion of the gain is calculated on a daily basis with only the post 6th April 2015 proportion being taxable. No valuation is required for this method, but an election must be completed.

Retrospective Basis

The entire gain/loss is chargeable, not just the post 6th April proportion. Again, an election is required and this method will be most beneficial where the disposal results in a loss as the entire loss would then be available to offset against other gains. Although because other gains would only crystallize when an individual resumed UK residence and so in reality, the use of the loss might be limited.

TAX PAYABLE

If the seller is registered for Self-Assessment, they can opt to pay the CGT due at the usual payment date on or before 31st January following the end of the tax year in which the gain arose, so for the 2015/16 tax year, the payment date would be on or before 31st January 2017. The reporting of the gain must still be done within 30 days though.

If the seller is not registered to pay tax in the UK, the CGT must be settled within 30 days of the conveyance date also. The payment can only be made once the sale has been notified to HMRC and they have issued a reference to which payment should be allocated.

PENALTIES

Penalties will be charged if either the reporting of the gain or payment of tax is late.

SUMMARY

These rules came into force on 6th April 2015 and applied to individuals, partners in partnership, trustees and personal representatives of a deceased non-resident individual.

All sales of property must be reported to HMRC within 30 days of conveyance. Chargeable gains will be calculated to the extent they accrue post 6th April 2015. Tax may be payable within 30 days of the date of conveyance. Penalties will be charged on both late reporting and late payment of tax. An election for the basis of calculation of the gain or a valuation as at 6th April 2015 may be required and so in order to report within the very limited timescales, the gain position must be considered as early as possible during the sale process.

FROM APRIL 2019 – THE NEW RULES.

From April 2019 non-UK residents are now subject to UK tax on gains arising from direct or indirect disposals of all types of UK land and interests in UK property rich entities.

This is a significant expansion of the current Non-Resident Capital Gains Tax (NRCGT) rules mentioned above which apply in only limited circumstances to direct disposals of residential properties.

It therefore represents a fundamental change to the existing regime. This is a topic that will impact all overseas investors in UK property, including real estate funds.

Unless an exemption applies, a non-resident will be subject to UK tax on gains arising from disposals made on or after 6 April 2019 of:

- Interests in UK land; and
- Interests in entities deriving at least 75% of their value from UK land (i.e. 'UK property rich' entities) where the investor has a 25% or more interest in the property rich entity.

However, the 25% de minimis will not be applicable in the case of interests in UK property rich collective investment vehicles (CIVs) (see below).

Where someone makes a chargeable disposal, they must report this disposal and make a payment on account of the capital gains tax due **still** within 30 days.

To ensure that only gains in respect of appreciation in value after 6 April 2019 are subject to UK tax, there will be a rebasing for tax purposes for both direct and indirect interests in UK land on 5 April 2019. It will however be possible to elect for historical cost to be used when calculating gains, where this is greater than the 5 April 2019 valuation. For indirect disposals, where historical cost is used and it gives rise to a loss rather than a gain, the loss is not allowable for offset against any other gains.

Whilst I understand that HMRC will not necessarily require formal valuations to have been undertaken at 5 April 2019, I recommend that investors consider what valuation evidence they have available to support April 2019 valuations, if it is possible to value both direct and indirect interests in land and whether this needs to be bolstered.

I expect that such valuation evidence will be important in the case of a future challenge from HMRC and/or in the case of a due diligence where a property rich entity is disposed (e.g. when negotiating a latent capital gains tax discount with a future purchaser).

Applicable Tax Rates.

Non-residents realising chargeable gains post 5th April 2019 will be taxed as follows:

- Non-resident companies will be subject to corporation tax at 19% (17% from April 2020)
- Non-resident individuals disposing of non-residential property will be subject to capital gains tax at 10% or 20%, depending on their marginal rate. Gains realised on disposal of residential property will be subject to capital gains tax at 18% or 28%, depending on their marginal rate.
- Non-resident trusts disposing of non-residential property will be subject to capital gains tax at 20%; whereas gains realised on disposal of residential property will be subject to capital gains tax at 28%.

Available Exemptions.

Certain classes of investors will be outside the scope of NRCGT, including sovereign immune investors and overseas pension schemes that meet specific criteria. In addition, qualifying institutional investors (QIIs) that qualify for enhanced relief under the Substantial Shareholdings Exemption (SSE) rules will be able to benefit from relief from NRCGT where they (or entities owned wholly/partly by QIIs) dispose of UK property rich entities (with no requirement for the entity to be trading), provided the SSE conditions are met.

QIIs include registered pension schemes, life assurance businesses, sovereign wealth funds, charities, investment trusts, authorised investment funds and exempt unauthorised unit trusts.

Interaction with tax treaties.

HMRC recognises that the UK's taxing rights under certain double tax treaties may not allow the UK to tax all non-resident investors (depending on their jurisdiction of residence) on gains that they realise from the disposal of UK property rich entities.

Whilst this is unlikely to be the case for direct disposals of UK land, there are certain tax treaties that do not include a securitised land provision, and hence do not allocate taxing rights to the UK for gains realised on the disposal of property rich entities. The most notable tax treaty that does not currently have a securitised land provision allocating taxing rights to the UK is the UK-Luxembourg treaty, however we understand that this is currently being re-negotiated.

Anti-forestalling rules apply and will allow HMRC to counteract tax advantages arising from the provisions of double tax treaties, where the tax payer has entered into abusive arrangements (from November 2017).

Collective Investment Vehicle (CIV).

HMRC has responded to the property industry's concerns about inequitable results for collective investment vehicles, by creating a specific subset of rules to determine how the NRCGT rules should apply to UK property rich CIVs. The purpose of these rules is broadly to exempt gains on disposals made by CIVs but to tax the investors on the disposal of their holdings in the CIV. The definition of a CIV is broad and includes the following:

- Collective Investment Schemes as defined in s235 FSMA 2000, including limited partnerships Alternative Investment Funds per Reg 3 AIFMR 2013 (SI 2013/1773)
- UK REITs
- Non-resident companies with features similar to UK REITs

Entities that fall to be CIVs per this definition will by default be treated as companies for the purposes of the NRCGT rules, with the exception of partnerships.
A CIV will be treated as property rich where a disposal of an interest in that CIV would be treated as a disposal of a UK property rich asset, deriving 75% or more of its value from UK property. Investors in UK property rich CIVs will not benefit from the 25% de-minimis ownership exemption, such that all disposals of interests in UK property rich CIVs will be within the scope of NRCGT (subject to the availability of any relevant exemptions).

ULTIMATE SUMMARY.

Non resident CGT rules have become a lot more complicated since April 2015. Please seek professional guidance well before you consider any UK property/land disposals.