CGT on non-residents selling UK residential property

What the latest Government response means for developers and investors

The Government has published more details of its plans for non-UK residents to pay capital gains tax (CGT) when they dispose of UK residential property.

The headlines are:

- confirmation that the Government does not intend to broaden the scope to tax non-residents on commercial real estate investments;
- the tax is only intended to apply to investors so trading profits should continue to be dealt with under the existing tax rules;
- communal residential property, such as care homes and "purpose built" student accommodation will be exempt;
- non-UK companies and funds that are widely held will be exempt;
- non-UK companies that are taxed under these new rules will be taxed at 20%, subject to indexation;
- but the ATED-related CGT charge will remain so some non-UK companies will continue to be taxed under those rules at 28%;
- non-UK resident individuals will be taxed at 18% or 28% depending upon what other UK income and gains they have;
- a modified principal private residence relief (PPR) will be available to non-resident individuals, which will require them to spend a minimum number of days living in their UK properties;
- group companies will be able to pool their relevant gains and losses from UK residential property; and
- only gains accruing post-April 2015 will be taxed. Non-residents who already own UK residential property will be able to "rebase" to the April 2015 market value or time apportion the gain.

Some of these points are discussed in more detail below.

Student and other communal accommodation

Care and nursing homes will be exempt, although assisted living accommodation will be within the scope of the charge (subject to PPR being available).

Student accommodation will also be exempt, but only if it is purpose built. For privately managed blocks this will mean a building:

- purpose built (or converted) for use by students;
- which consists of at least 15 bedrooms (which can be either standalone units or within cluster flats or a mixture); and
- occupied for more than 50% of a tax year by students for the purpose of attending a course. So a certain amount of holiday lettings for e.g. conferences should be possible (although note that such use can affect the VAT treatment).

This is a narrower test than the one used in the VAT rules. It is intended to cover only larger student accommodation blocks and not, for example, private homes used by students.

Most accommodation that is directly controlled or managed by the educational institution itself should also be exempt even if it does not fall within the above definition of "purpose built".

Issues for developers

At the moment a property can only be subject to CGT when it is held as an investment. The Government says that these changes should not, therefore, affect non-UK residents who sell trading stock. However, it has also decided that "off plan" sales will be taxed under these new rules in the same way as a completed property.

Given that almost all "off plan" sales will be trading (and so not subject to CGT), it is not clear what the Government is targeting. Notwithstanding the Government assurances we will be reviewing the draft legislation carefully to check how it could offshore traders.

Developers who are intending to hold onto the completed property as an investment will definitely be within the scope of these rules, even

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if they decide to sell the property whilst they are still building it. However, sales of bare land will not be caught unless construction has started.

Developers (UK or non-UK) who are marketing to non-UK residents will need to be aware of the changes to PPR as this will affect whether potential buyers will be subject to UK tax on their home.

PPR relief exempts the gain realised on the disposal of a person's only or main residence from CGT. Where a person has more than one residence he can currently elect which is to be treated as his main residence for the purposes of PPR relief. If the rules remained unchanged this would mean that a non-resident subject to the new CGT charge would be able to elect for their UK home to be treated as their main residence and so avoid CGT on it.

The availability of PPR relief is, therefore, being restricted. From April 2015 non-residents will only qualify for PPR relief on their UK home if they spend 90 midnights at that home (or another UK home) each tax year.

Although this will offer some non-residents a route to escape the charge, spending 90 nights in the UK will result in the individual having another "UK tie" for the purposes of the UK's statutory residence test. This may tip the person into being treated as UK tax resident and potentially subject to UK tax on their worldwide income and gains.

For married couples/civil partners occupation by one spouse/civil partner will be regarded as occupation by the other. This means that where one spouse is resident and the other non-resident, the non-resident spouse's share of the UK home can qualify for PPR relief without the non-resident having to meet the "90-midnight" rule.

Exemptions to encourage investment in UK residential property

One of the concerns about introducing CGT on non-residents is its effect on inward investment into the UK residential sector generally. The Government, therefore, intends that widely held funds and other investment vehicles should be exempt from the charge.

In relation to non-UK companies, the Government will introduce a "narrowly controlled company" test. This will be similar to the existing "close company" test (controlled by five or fewer persons) but with two notable improvements:

- removing a bear trap that catches any company owned by a partnership; and
- looking through shareholders that are "qualified institutional investors". So a company should not be caught by these rules if it is majority owned by e.g. a fund, a sovereign wealth fund or a REIT.

Note that this new tax charge will only apply to direct sales of UK residential property. The sale of a SPV that already holds a property should not be caught.

In relation to non-UK funds, a collective investment scheme will be exempt from these rules if it satisfies the existing "genuine diversity of ownership" test. Broadly, this means it must be open and marketed to a sufficiently wide class of investors.

Foreign REITs that are equivalent to a UK REIT will also be exempt.

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