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Alan McGuiness
Specialist Personal Tax
Assets and Residence Policy
HM Revenue and Customs
100 Parliament Street
London SW1A 2HQ

Dear Mr McGuiness

Consultation on non-residents capital gains charge

Introduction

Executive Summary

- We agree in the move to add fairness to the system and, as such, believe capital gains tax should apply to all types of property and not be dependent on whether or not the owner is UK tax resident or not. This would give a simple system and avoid directing investment away from residential to commercial properties.

- A self-assessment system based on the non-resident landlords scheme is preferable to a blanket withholding tax on all transactions. This can be backed up with a secondary tax charge on purchasers of UK properties to ensure compliance.

- Detailed work is required to ensure tax exempt investors are not subject to tax even if investing through several levels of a structure and also that there is no double taxation for taxpayers.

- ATED CGT charge should be abolished to avoid complications.

- The legislation should, as far as possible, utilise existing definitions, rules and rates to avoid creating unexpected tax planning opportunities.

Overall Aims & Structure

The overall aims of this proposal, to create a fair and simple tax system for UK property are to be applauded and encouraged.

The UK needs to continue to be seen as open for business and welcoming investment from both the UK and overseas. As part of this the taxation system need to be fair and easily understandable to all investors.

From an investors perspective it is important to have certainty when investing. Therefore continual small changes, as experienced in the last few years, to the tax system can be more harmful to inward investment than a simple tax applied fairly to all.

The only logical conclusion based on the objectives of fairness, sustainability and simplicity set out in the opening statement of the consultation is to extend the CGT charge to non-residents investing in all UK property.

By implementing the charge to all property now it will give the following benefits:

- Certainty of tax position
  - All investors in the UK will know what their tax position is going to be.
  - Investors already expect at some point the UK Exchequer will tax all UK property in line with the majority of other countries in the world. This risk is now starting to be priced into transactions.
- Fairness
  - UK resident corporate investors, who are not a REIT, are currently at a disadvantage in buying UK properties.
  - CLS Holdings pays UK corporation tax on its gains, whereas offshore investors suffer no tax.
- Increase in tax receipts for the UK Treasury.
  - The additional tax revenue could be used to offset costs relating to a fundamental reform of the business rates system.
- Increased jobs in the UK
  - CLS supports jobs in the UK, and therefore pays income tax and national insurance. Some of these jobs would be offshore if the properties were held offshore as is currently encouraged by the tax legislation.
  - This will reduce the cost and complexity of holding UK properties through offshore structures.

- Simplicity
  - There will be no need to define residential / non-residential / communal properties.

Arguments will be put forward by others that extending the scope of CGT will reduce foreign investment in UK property. However, these arguments are flawed for a number of reasons.

- Investments in UK property are based on UK property market fundamentals
  - CGT will be levied only on profits.
  - Tax rates in the UK are now competitive with other developed nations.
  - Very few other countries give such generous exemptions to overseas investors and those countries still receive significant investment in their property sectors.
  - SDLT at 4% is a larger disincentive for investment in UK property as this is a permanent upfront cost which is not dependent on whether profits have been made.
- UK property is attractive due to the rule of law and security
  - The strong governance and legal system in the UK means the property investment in the UK is a safe investment.
  - It is fair that non-residents should be subject to tax on capital gains to maintain these public goods available in the UK, but not in some other countries.
- Onshore investment options are available.
  - Tax exempt investors already have a number of options for investing in the UK.
  - Structuring opportunities such as REITS and PAIFs exist to ensure an equitable outcome for other investors

Attached is a detailed response to the consultation. I am happy to discuss these points in more detail if you require.

Yours sincerely

APPENDIX 1

Responses to specific queries

1. Exclusion of communal property.
    - This exemption will complicate the legislation and should be avoided if possible.
    - The definition of communal property is likely to lead to significant confusion and legal challenge. For example how will the following student developments be distinguished
        - University owned hall of residence on a university campus
        - Student building on campus but owned and managed separately
        - Student accommodation as above but adjacent to the main university site.
        - Student accommodation offsite but with a long-term nomination agreement from a particular institution
        - Student accommodation rented directly to students from a specific institution
        - Student accommodation rented to any students with shared communal facilities such as common rooms.
        - Accommodation with shared facilities let to students and non-students.
    - Similar problems will arise from aged care and health facilities.
    - It would be preferable to manage any charge to capital gains through existing exemptions and reliefs to the capital gains tax charge rather than having an exemption for a type of property. For example particular investors being treated as exempt e.g.
        - Charities
        - Social landlords
    - Giving a different set of exemptions to non-resident investors in certain types of properties will continue the current unfairness and give opportunities for tax planning and lead to a distortion in the market e.g. properties being redesigned to meet the exemption.

2. No comment as this exemption should not be required.

3. No comment.

4. No comment.

5. Genuine diversity of ownership

    There should be consideration given to which types of entities this exemption is trying to cover. It would not seem appropriate to give listed non-UK resident companies a tax advantage over listed UK resident companies, whereas we agree that genuine funds of tax exempt investors should remain exempt.

    If this option is decided upon, it should for simplicity use existing, well understood, rules such as those for a Close Company.

    Investment through offshore Property Unit Trusts is a regular way of investing in UK properties. This allows investors with different tax attributes to hold properties without disadvantage. For example, at present many UK companies hold investments in a Jersey Property Unit Trusts. The income on these properties is subject to UK tax, however capital gains within the JPUT are not subject to tax. If these gains are distributed out of the JPUT, or the units in the JPUT are sold there would be a tax charge on the sale of the units.

    If the JPUT was subject to tax on property disposals, there would be an effective double taxation charge when the profits are distributed back to the UK. (i.e. at the property and unit level).

    Therefore, the tax status of these types of entities would have to be reviewed. One solution for this would be to treat the gains in the same way as partnerships and have the gains attributable to unit holders directly.

6. Practical difficulties
   From the start a targeted general anti avoidance rules for this would be useful, including the ability to get clearance for specific circumstances.

7. No comment.

8. Impacts of charging gains on residential property held by non-resident property companies.
   - The interaction of the new rules with ATED CGT charge will be complicated based on a number of different scenarios.

     Properties held by non-residents could be subject to CGT ATED properties for some part of their ownership and this extension of CGT for non-residents for another part of the gain.

     Assuming the extension to CGT comes into effect from 1 April 2015. A property held by a non-resident company, purchased pre 1 April 2013 valued at below £500,000 on 1 April 2015. At this point it would not be subject to ATED. If the value on 1 April 2016 is above £500,000 the property would be subject to ATED CGT from that point.

     On disposal there would be the following:
       - Any gain or loss pre 6 April 2013 would not be subject to any tax
       - AETD CGT charge at 28% on the proportion of the gain since 1 April 2016 when the property was subject to ATED
       - The remaining gain, above the valuation at the date of this extension of CGT to non-residents, that is not subject to the ATED CGT charge would be subject to tax at the corporate tax rate, say 20%.

     This is extremely complicated and would require 2 valuations without third party contemporary transactions (i.e. 1 April 2016 and on introduction of this extension.)

     There would also be the complication of properties passing in and out of the ATED regime over their period of ownership depending on their value or whether they qualify for an exemption or not.

     The CGT charge part of ATED will not raise significant revenue as it would only change the effective tax rate from 20% to 28% of any gain. Therefore the ATED CGT charge should be removed when this is introduced.

   - HMRC compliance processes for non-resident companies needs to be improved.
       - Ability to file Non Resident Landlord returns online
       - Preferably the NRL returns would include a section for chargeable gains to limit multiple filing obligations.

9. No comment.

10. Changes to PRR rules
    The proposed changes to the PRR rules have the risk of adversely impacting UK residents. At present certainty for UK residents is achieved over their main residence by this election.

    It would be simpler to only allow an election of a UK main residence in the tax years, or part of tax years, that the individual is a UK tax resident. Therefore for an individual who emigrates the PRR would apply for his time in the UK, but not for the time when he is a non-resident.
    If an individual is not a UK resident then the UK property cannot be their main residence.

11. See Q10 above.

12. See Q10 above.

13. Withholding tax on non-resident disposals

    We do not believe it is practical to implement a withholding tax system as the UK legal system does not have a 'gatekeeper', such as a notary, for property transactions. It would be possible for two offshore investors to transact without any UK solicitor or accountant, therefore there would still be no protection for the UK exchequer for deliberate non-compliance.

    Also, a flat withholding tax rate based on the sales price could heavily penalise some sales where, due to losses, the debt on the property is larger than sales price.

    <u>Alternative option</u>

    It would be possible to put a secondary responsibility on paying the capital gains charge on to the purchaser of the property. This secondary responsibility is secured in the UK as the property is based in the UK and could be enforced, in extreme circumstances, by repossession of the property.

    It would be possible for purchasers to protect themselves from risk of the vendor's non-compliance by placing part of the consideration in escrow, to cover the expected tax liability in until it is settled with the HMRC. This has the advantage of not requiring any additional systems for HMRC to manage withholding tax payments and refunds of filing requirements for solicitors or accountants. It would give an effective withholding of the tax by the purchasers solicitors in the escrow account. The amount of this would be negotiated directly between the purchaser and the seller based on the circumstances of each transaction (e.g. depending on whether the vendor has made a loss), therefore avoiding complications for lossmaking transactions.

    It would also be possible to give an exemption to this secondary responsibility on the purchasers if the vendor had a 'tax clearance certificate' from HMRC.

    These certificates could be issued to UK tax payers or non-resident landlords who have had a good history of compliance. This would favour good tax-payers and encourage wider compliance with all taxes. It should also be able to avoid any complication with the EU non-discrimination principle.

14. – 16 See Above

<u>Groups of companies</u>

Finally, there would also have to be consideration given to groups of companies. Rules similar to s171 TCGA 1992 would be required to ensure that group reconstructions are not subject to tax. For example:-

- Transferring a UK property from a non UK resident company to a UK resident company within a group.
- Transferring a UK property from a UK resident company to a non-UK resident company within a group.
- Transferring a UK property between two non UK resident companies.

Consideration should also be given to transfers from partnerships or collective investment schemes.

De-grouping provisions similar to s179 TCGA 1992 would also be required.