

# **How will the Budget affect your Property business?**

**Tuesday 29 March 2011**

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# Income tax rates

	2010/11	2011/12
Personal allowance	£6,475	£7,475
Income limit	£100,000	£100,000
Basic rate – 20%	£37,400	£35,000
Higher rate – 40%	£37,401 - £150,000	£35,001 - £150,000
Additional rate – 50%	> £150,000	> £150,000

Note personal allowance for 2012/13 will be £8,015



# National insurance rates

	2010/11	2011/12
Employer's NIC	12.8%	13.8%
Employee's NIC 2011-12 £7,228 to £42,484	11%	12%
Employee's NIC 2011-12 over £42,484	1%	2%
Class 4 NIC	1%	2%



# Capital gains tax

	2010/11	2011/12
Annual exemption	£10,100	£10,600
Basic rate tax payers	18%	18%
40% & 50% tax payers	28%	28%
Entrepreneurs' relief – 10%	£5 million	£10 million
Trust capital gains tax rate	28%	28%



# Corporation tax rates - 2011/12

	Originally announced 2009	Announced 2010	Budget 2011
Small company	22%	20%	20%
Marginal company	29.5%	28.75%	27.5%
Large company	28%	27%	26%



# Effective marginal tax rate

	Small company	Marginal company	Large company
Salary	57.82%	57.82%	57.82%
Dividend	48.89%	53.68%	52.72%
Interest or rent – No NI $\Omega$	50%	50%	50%
$\Omega$ Note impact on entrepreneurs' relief			
Self employment	52%	52%	52%



# Effective tax rates on extracting profits

## April 2011/12

### UK resident – 50% tax rate payer



	LLP Personal CGT Gain	Personal Income Trading	Corporate Liquidate Investment	Corporate Liquidate Trading	Corporate Dividend	Salary
<b>Marginal top rate</b>						
Gain / Profit	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Corporation Tax 26%			260,000	260,000	260,000	
Salary						878,735
ERS NI - 13.8%						121,265
<b>Post tax profit</b>	<b>1,000,000</b>	<b>1,000,000</b>	<b>740,000</b>	<b>740,000</b>	<b>740,000</b>	<b>1,000,000</b>
<b>Dividend / Salary</b>					<b>740,000</b>	<b>878,735</b>
Highest rate tax	280,000	500,000	207,200	74,000	267,222	439,367
NI EES 2%		20,000				17,575
<b>Net available to spend</b>	<b>720,000</b>	<b>480,000</b>	<b>532,800</b>	<b>666,000</b>	<b>472,778</b>	<b>421,793</b>
<b>Effective rate of tax</b>	<b>28.00%</b>	<b>52.00%</b>	<b>46.72%</b>	<b>33.40%</b>	<b>52.72%</b>	<b>57.82%</b>



# Effective tax rates on extracting profits in the future UK resident

## Tax if top rate falls to 40%



	LLP Personal CGT Gain	Personal Income Trading	Corporate Liquidate Investment	Corporate Liquidate Trading	Corporate Dividend	Salary
Marginal top rate						
Gain / Profit	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Corporation Tax 26%			260,000	260,000	260,000	
Salary						878,735
ERS NI - 13.8%						121,265
Post tax profit	1,000,000	1,000,000	740,000	740,000	740,000	1,000,000
Dividend / Salary					740,000	878,735
Highest rate tax	280,000	400,000	207,200	74,000	185,000	351,494
NI EES 2%		20,000				17,575
Net available to spend	720,000	580,000	532,800	666,000	555,000	509,666
Effective rate of tax	28.00%	42.00%	46.72%	33.40%	44.50%	49.03%



# Effective tax rates on extracting profits after April 2014 UK resident

## Top if top rate falls to 40%

	LLP Personal CGT Gain	Personal Income Trading	Corporate Liquidate Investment	Corporate Liquidate Trading	Corporate Dividend	Salary
<b>Marginal top rate</b>						
Gain / Profit	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Corporation Tax 23%			230,000	230,000	230,000	
Salary						878,735
ERS NI - 13.8%						121,265
<b>Post tax profit</b>	<b>1,000,000</b>	<b>1,000,000</b>	<b>770,000</b>	<b>770,000</b>	<b>770,000</b>	<b>1,000,000</b>
<b>Dividend / Salary</b>					<b>770,000</b>	<b>878,735</b>
Highest rate tax	280,000	400,000	215,600	77,000	192,500	351,494
NI EES 2%		20,000				17,575
<b>Net available to spend</b>	<b>720,000</b>	<b>580,000</b>	<b>554,400</b>	<b>693,000</b>	<b>577,500</b>	<b>509,666</b>
<b>Effective rate of tax</b>	<b>28.00%</b>	<b>42.00%</b>	<b>44.56%</b>	<b>30.70%</b>	<b>42.25%</b>	<b>49.03%</b>



# Message

- Structures that minimise income tax now and allow income / gains to be sheltered for the next few years are beneficial
- Capital Gains still delivers low tax rate at 10% for entrepreneurs relief and 28% top rate



# Inheritance tax

	2010/11	2011/12
Nil rate band	£325,000	£325,000
Life time gifts	20%	20%
On death	40%	40%

From April 2012 – 10% reduction in tax rate on death where  $\geq 10\%$  of net estate left to charity



## Example

	£ 2001-11	£2011-12	£2011-12
Net estate after liabilities & costs	1,000,000	1,000,000	1,000,000
Legacy to The Red Cross	100,000	nil	100,000
Nil rate band	325,000	325,000	325,000
Estate taxable at 40%	575,000	675,000	575,000
Inheritance tax at 40%	230,000	270,000	
Inheritance tax at 30%			<del>172,500</del>
Inheritance tax at 36%			207,000
<b>Net to Beneficiaries</b>	<b>670,000</b>	<b>730,000</b>	<b>693,000</b>

# Non-domiciled individuals

- Currently if you claim the remittance basis:
  - Lose personal allowance
  - £30,000 tax charge if you have been UK resident at least 7 out last 9 years
- The above does not apply if unremitted income & gains < £2,000



# Non-domiciled individuals

- Proposal from 6 April 2012:
  - Resident for > 12 years – charge becomes £50,000
- Where income or gains remitted for purposes of commercial investment in UK businesses, the charge will not apply – probably not property!



# Non Domiciled

- Note...Very rough proposals
- Ill defined
- Are gains on UK investments then taxable as UK gains rather than being tax free if invested from abroad?
- “Coach & Horses” maybe possible to invest then liquidate
- Must wait the legislation due 31 March 2011



# Non domiciled investors / off shore / non close investor

- Non Resident Landlord Provisions of 20% tax on net rental income and tax free gains still best route for holding investment property in the UK
- Always examine investing parties to see if can benefit from this regime
- Often UK residents entity can benefit from these provisions
- JPUTs etc still on the agenda



# EIS & VCTs

- Incentives for investing in new & growing businesses
- Creates demand for Commercial Property
- Good for property businesses



## EIS & VCTs

- All changes subject to State Aid approval
- From 6 April 2011:
  - Rate of income tax relief for EIS 20% → 30%
- From 6 April 2012:
  - Employee limit < 250 (50)
  - Gross asset limit ≤ £15M before investment (£7M)
  - Maximum annual amount raised £10M (£2M)
  - Maximum annual investment £1M (£500K)



## EIS – 3 reliefs

- Income tax relief
- Capital gains tax exemption
- Capital gains tax deferral
  
- BUT Property in most forms is excluded may get services to sector but generally not for property sector



# Enterprise Zones

- Introduced by Margaret Thatcher
- 21 new Enterprise zones created, 100% tax relief on cost of constructing industrial buildings,
- Tenant up to 100% rates relief
- Areas announced to include:- Croydon, Tottenham,



# Stamp Duty Land Tax

- Pre budget announcement - SDLT avoidance schemes listed as believed to be ineffective
- Believe HMRC used major law firm to prove many schemes did not work
- HMRC now challenging SDLT1 forms submitted in last 9 months
- Many providers of SDLT planning saying pay up!
- Some providers saying new scheme's still work



# Stamp Duty Land Tax

- New average rate for bulk purchase of residential property to encourage funds to enter market
- Previously on aggregate cost of all property acquired simultaneously, 5% from 1 April 2011 over £1 million
- Now calculated on average property multiplied by number of properties
- 200 units at £100k was £1million now £200k



# High risk avoidance schemes

- HM Revenue & Customs perceives that there is a cash flow advantage to tax schemes even if they fail
- List specific schemes in regulations
- A range of options to ensure users do not benefit from retaining the tax in dispute!
- Encouraged to pay the tax earlier
- Additional charge for late payment if tax is due



# Disguised remuneration

- Draft Part 7A
- Design to prevent directors & employees using third party arrangements to avoid tax
- Typically involves:
  - Employment benefit trust (EBT)
  - Employer funded retirement benefit scheme (EFURB)
  - Qualifying non-UK pension scheme (QNUPS)



# Disguised remuneration

- Previously able to make a profit and then use EBT's, EFURBS, QNUPS to pay profit into off shore.
- Tax deduction in Company and a loan back of all cash with no tax charge. HMRC always contended did not work but did not attack in courts but understand now will attack
- Message is PLAN AHEAD not after the event



# The basics for the employee

- New rules apply from 6 April 2011
- Existing loans (pre-9 December 2010 loans appear to escape) unless they need to be repaid & re-advanced
- Loans made after 9 December 2010 & not repaid by 5 April 2012 are caught
- Liability to PAYE& NIC on the loan or asset provided



## Wide drafting???

- Employee commutes from Milton Keynes to London by train
- Another company in the group provides him with an interest free loan to buy a season ticket
- Draft rules say amount of loan subject to PAYE & NIC
- No refund when loan repaid!!!!



## Better example!!

.....suppose a holiday company charters a passenger aircraft with a market value of £20m for two weeks to take fee paying customers on holiday, but permits an employee to take an otherwise unused seat on the aircraft for his holiday. The airline is a third party and takes the 'step' of providing use of the aircraft to the employee. The employee is to be taxed on £20m



# Revenue response?

- Revenue produced FAQs on 21 February
- “We agree that Part 7A would have this unintended consequence”
- “As drafted, Part 7A could have that consequence”
- “The intention is to amend Part 7A”
- Amendments promised in Budget documents



## ...and the answer is?

- Review existing EBT, EFURB arrangements
- Take advice on new rules as they might apply to unintended transactions



# Real Estate Investment Trusts

## REITs

- Proposals for April 2012
- REIT conversion charge (2%) on value of gross portfolio to be scrapped, this was in lieu of capital gains tax but as market fallen no gains in many portfolio's.
- Relaxation in rules regarding holding cash to allow REITs to be more flexible in volatile markets, currently requirement to be 90% invested.



# Approved mileage allowance

- From 6 April 2011
- 40p → 45p per mile
- Free of income tax & NIC
- Passenger payment allowance 5p for employees
  - Now extended to volunteers
- Expenses are tax free.... Always claim everything.... Even if disallowed in business as long as for purpose of business very efficient.



# Entrepreneurs' relief

- For disposals on or after 6 April 2011
- Life time allowance increased for £5M to £10M
- Disposal in March 2011:
  - £6M gain
  - ER £5M & £1M at 28%
- Another disposal May 2011
  - £2M gain
  - ER – £2M with £3M of life time allowance unused



# Entrepreneurs' relief

- 10% tax rate
- Worth £1.8M now (originally only £80K)
- One limit each for spouses & civil partners (& children)



# Companies

- Trading company, companies & groups:
  - own at least 5% of ordinary shares which give at least 5% of votes; &
  - be an employee or directorfor at least 12 months prior to the disposal
- Do not have to own all the shares for 12 months
- Beware dilutions: e.g. acquisitions & share options



# How to miss out!

- Not being wholly a trade:
  - 20% non trading activity permitted
  - If a problem - do something about it
- Not owning shares or business or assets for 12 months:
  - Options?
- Not being an employee or director – care required



## How to miss out!

- Selling assets - not selling part of a business
- Letting property to a 5% company or business in which you are a partner etc
- Assets owned by a discretionary trust
- Assets owned by an interest in possession trust if life tenant does not qualify



# Old CGT Entrepreneurs relief planning

- Pre-election planning in 2010
- Created trusts to ‘bank’ entrepreneurs’ relief & 18% capital gains tax
- Should those structures now be unwound?
  - Break even point = gain of £17.2M?
- Generally all capital gains tax planning for businesses & business assets should be reviewed



# Capital allowances

- Annual investment allowance:
  - Reduced to £25,000 from 1 April/6 April 2012
  - Currently £100,000
- Short life assets:
  - Currently a 4 year cut-off point
  - To be extended to 8 years



# Enhanced capital allowances

- Energy saving technologies
- 100% first year allowances
- Updated list of technologies
- Now to include certain energy efficient hand dryers
- From – before summer recess
- [www.eca.gov.uk](http://www.eca.gov.uk)



## R&D tax credits - SMEs

- Subject to State Aid approval
- From 1 April 2011 – 75% → 100% of spend
- From 1 April 2012 – 100% → 125% of spend
- Other changes (subject to consultation):
  - £10,000 pa minimum spend will be abolished
  - Limiting repayable tax credit to amount of PAYE/NIC paid will be abolished
  - Changes to large company scheme - subcontractors



# ESC C16

Dormant company	
	£
Cash	<u>50,000</u>
Ordinary share capital	1,000
Retained profits	<u>49,000</u>
Shareholders' funds	<u>50,000</u>
Shareholder wants the cash out!	



# Alternatives

- Members' voluntary winding up:
  - Capital gains tax liability – 18% or 28%
  - Liquidator's fees £5,000 - £8,000
- Pay a £49,000 dividend:
  - Income tax on dividend
  - What about the share capital?



# Associated companies

- £300,000 & £1.5M limits divided by number of associated companies
- Companies under common control
- Attribute rights of relatives
- ESC C9 limits this attribution amongst relatives (excluding spouses & minor children) to situation where there is ‘substantial commercial interdependence’



# Furnished holiday lettings

- Minimum period property available for letting to public - 140 → 210 days a year from April 2012
- Minimum period property is actually let - 70 days → 105 days
- Losses made in a qualifying UK or EEA furnished holiday lettings business may only be set against income from the same UK or EEA furnished holiday lettings business



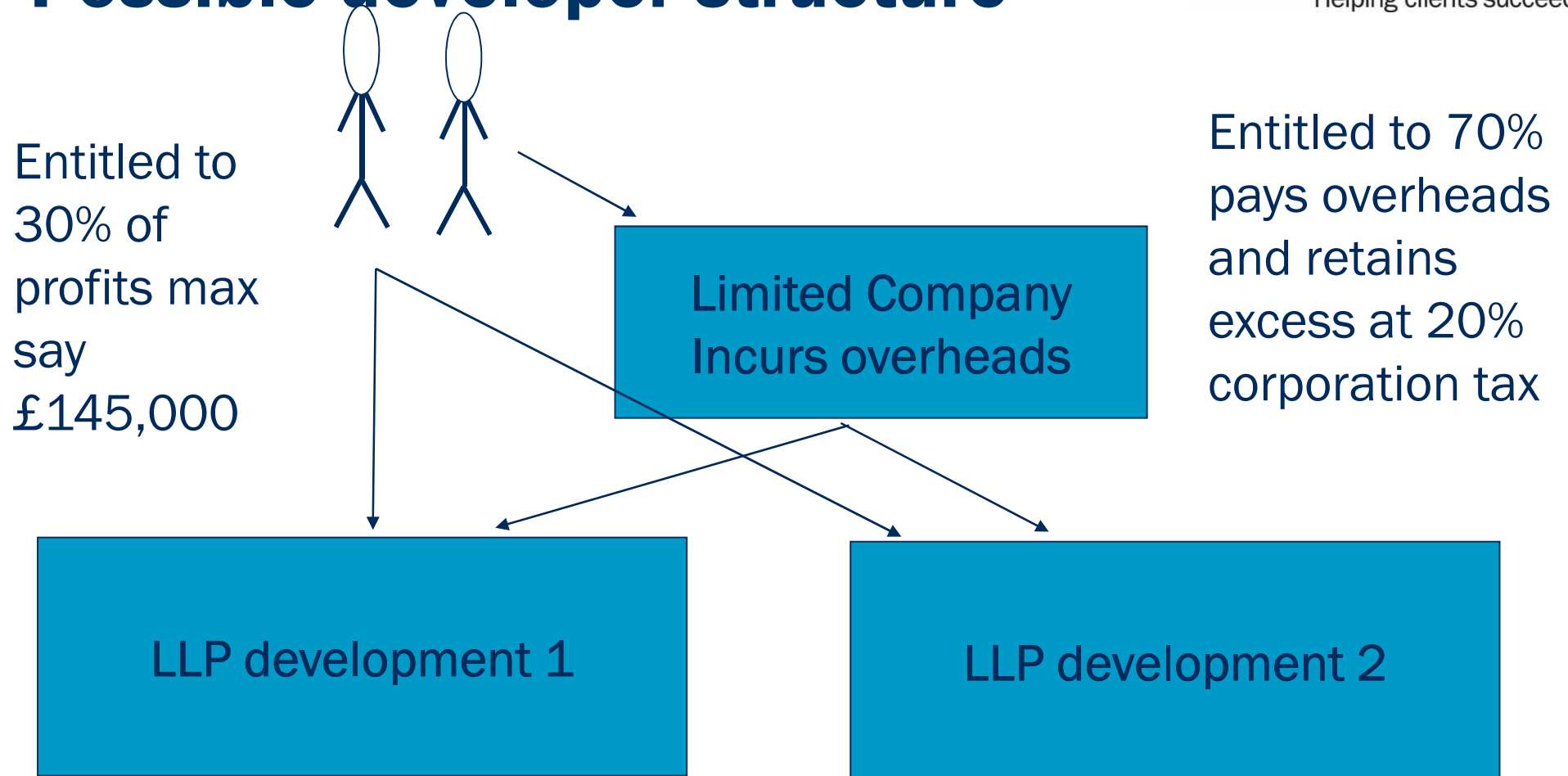
What should I consider now?

How should structure something in future?

What are others doing?



# Possible developer structure

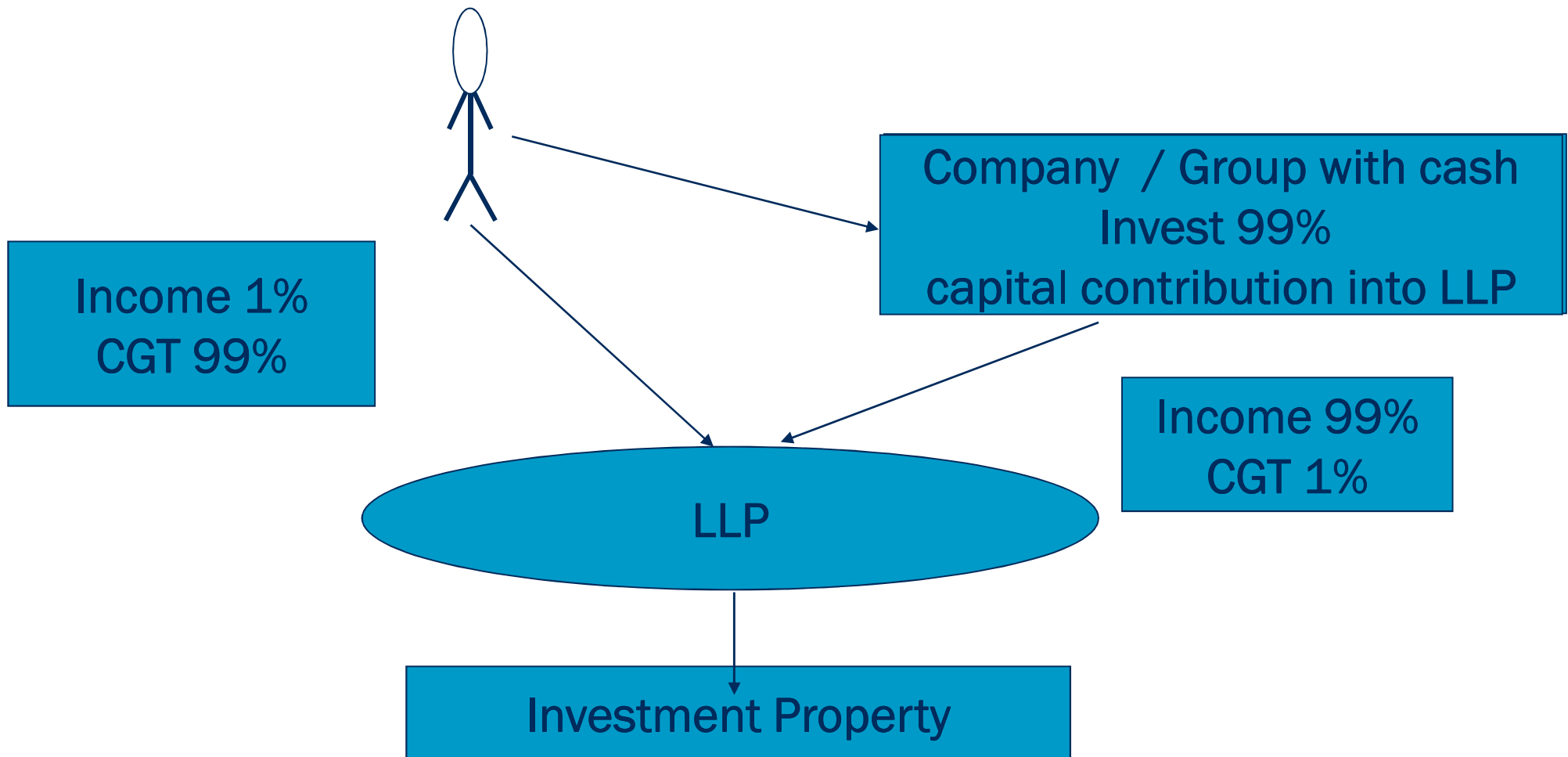


## LLP structure

- Greater thought needed if foresee profits over £150,000
- Introduce spouse to enable £299,999 at up to 40%
- Add companies into the equation, one service company and maybe equity providers
- How many companies? Multiple?



# INVESTORS – How to achieve CGT with a Company

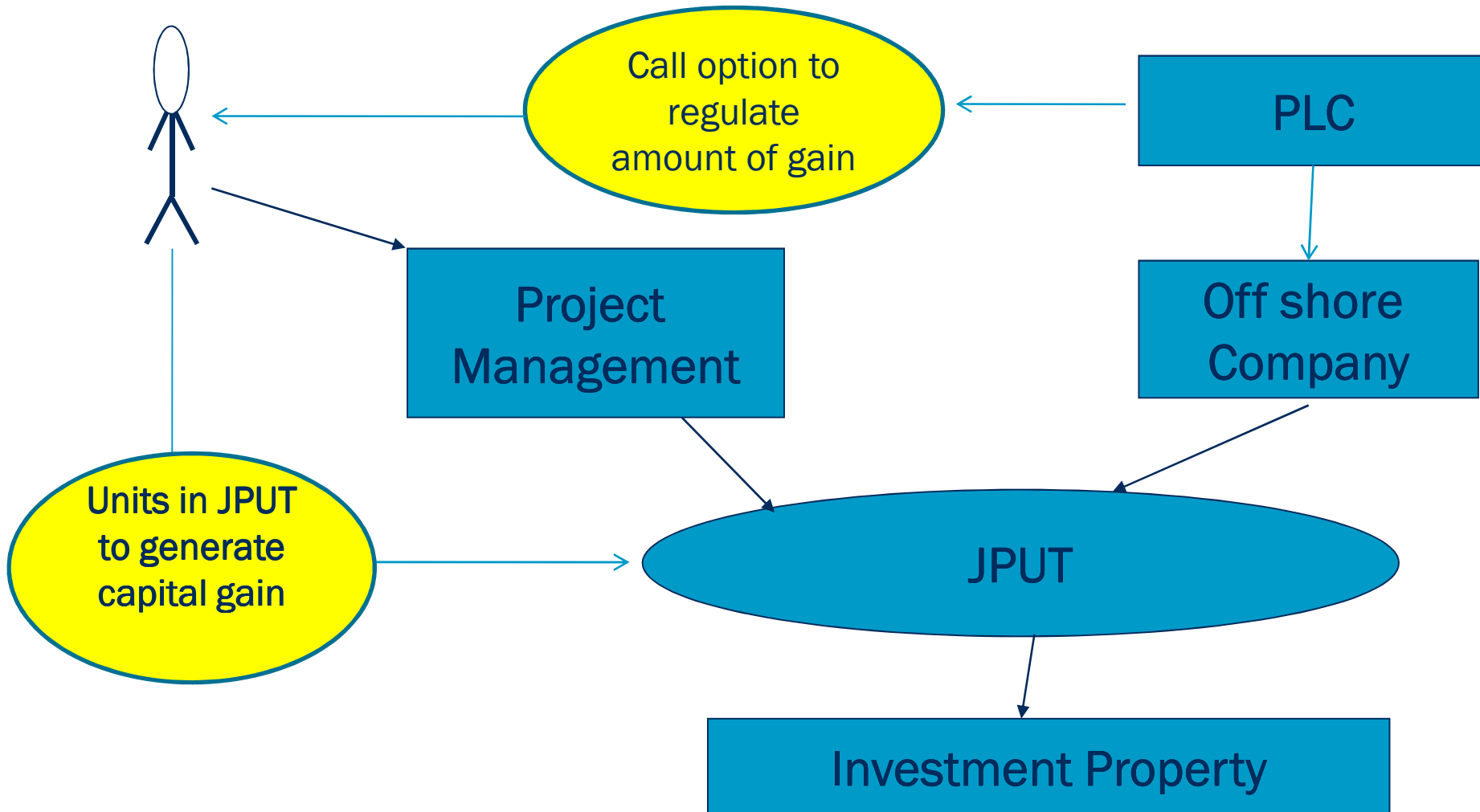


## CGT position on sale

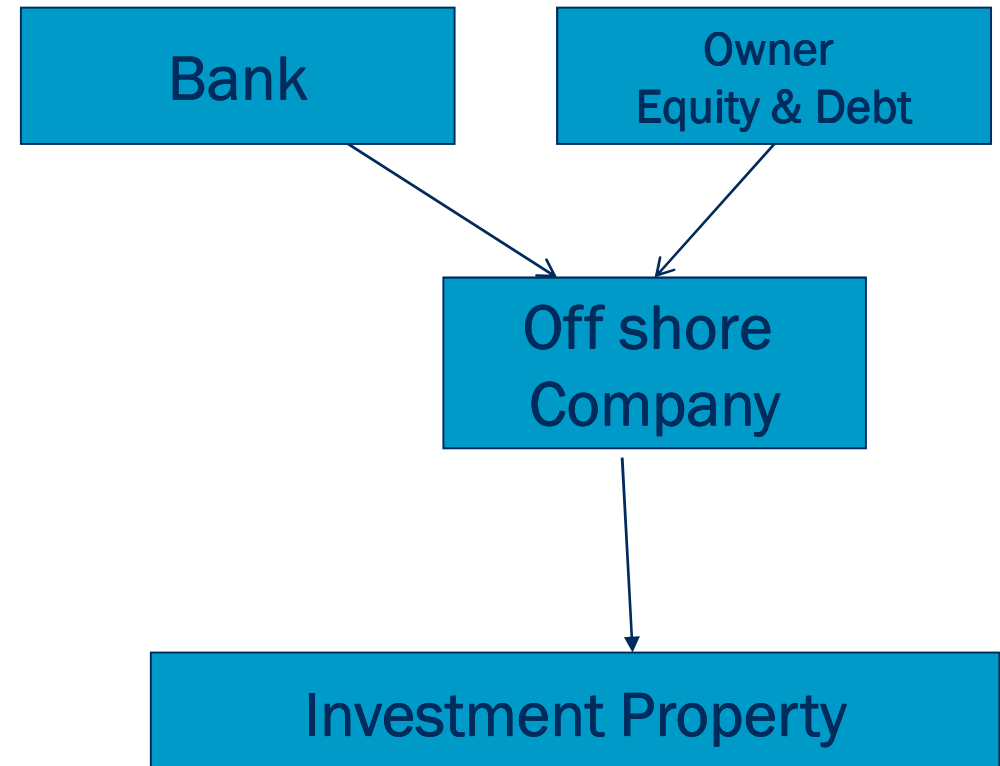
- A well drafted LLP Members agreement will recognise the different contributions made by the partners
- Company takes majority of income for providing majority of capital.
- Individuals charged with running and in exchange receive small income but enhanced capital profit on sale
- CGT on sale taxed at 28% and passes straight to individuals



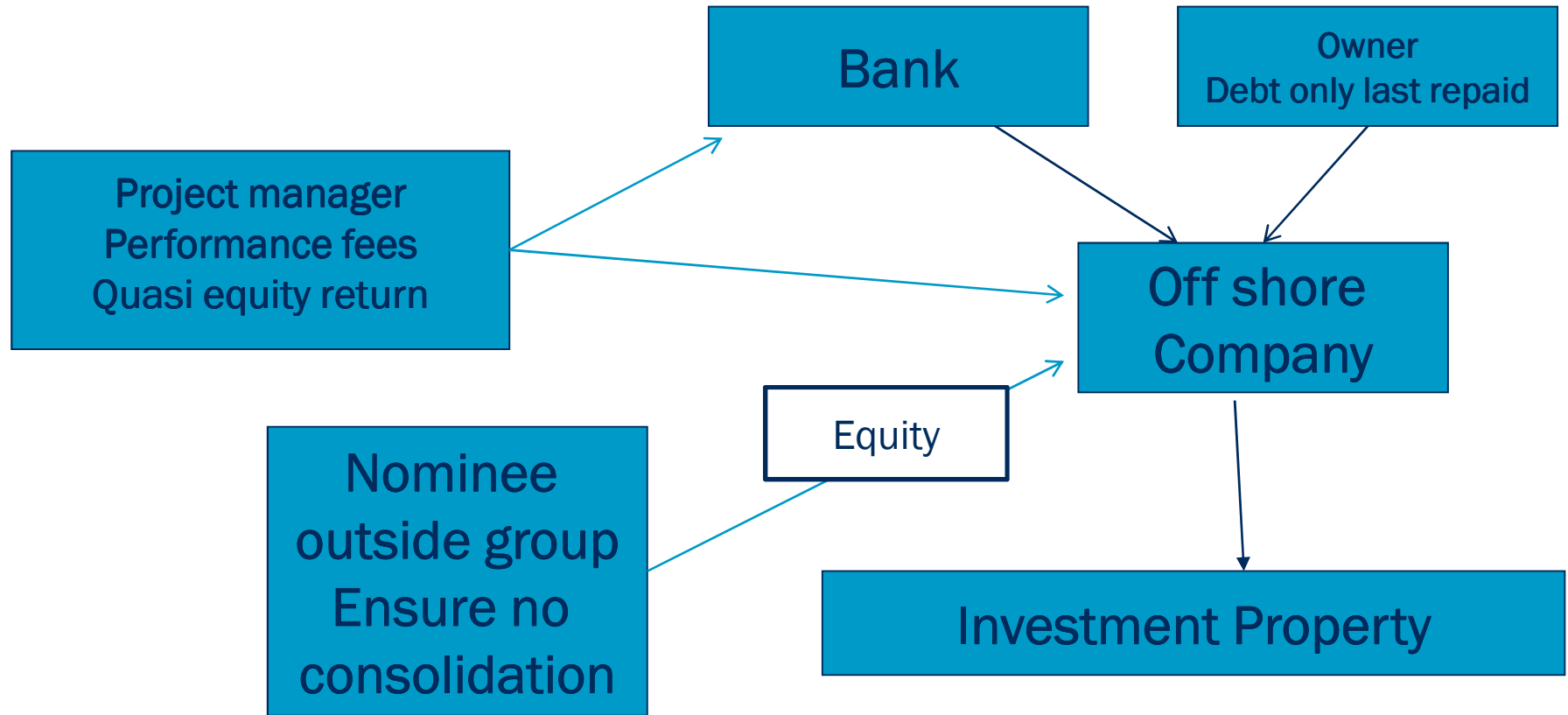
# A recent structure



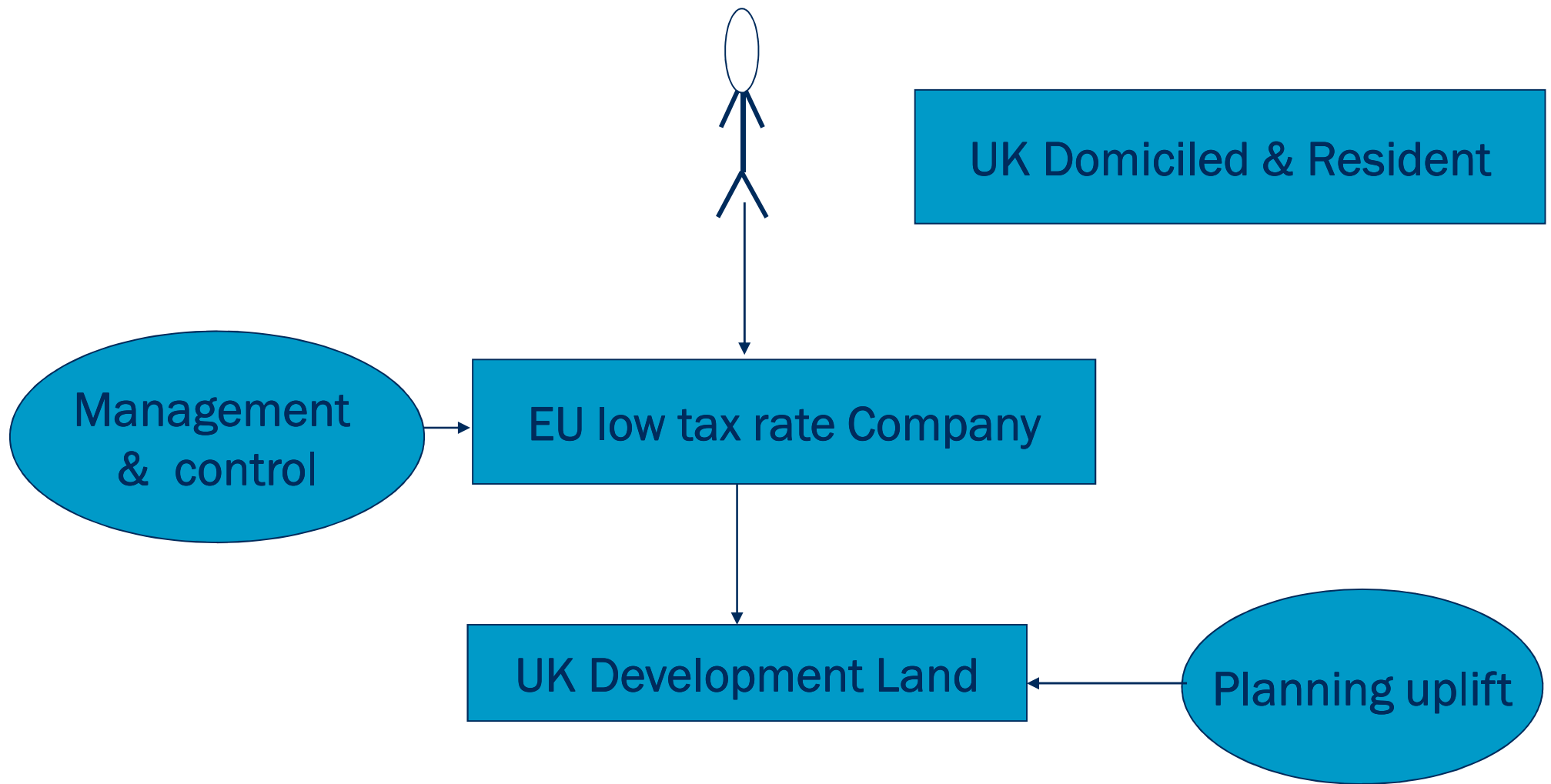
## A recent transaction - Problem



# A recent transaction - Solution



# EU trading structure



# Use of EU Company - trading

- Use EU company to generate planning uplift
- Sell property back to UK for development
- Reinvest via EU
- As trading profits avoids S714 (old S739) attribution back to UK domiciled individuals
- In time become non resident to UK for 1 year and take dividend
- Or pay UK CGT at Business Asset Rate if trading



# Cyprus Planning Gain Position

£000's	UK	Say Cyprus
Profit	5,000	5,000
Corp Tax (UK 2011)	1,300	500
Net profit	3,700	4,500
CGT at 10%	370	450
Net cash to investor	3,330	4,050



# VAT

- Always take advice!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!!
- Opting of tax rules are complicated
- If doing residential development, for future investment then consider design and build contractor to recover VAT on professional fees
- If building for investment consider separate contractor entity to accumulate services
- Worst tax to get wrong



**And finally....**

**....any questions?**



# Contact details



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