Investing in the UK real estate: tax aspects and planning considerations

After some years of continuing reforms and amendments to various aspects of property taxation, this article summaries up the most important tax rules, privileging a non-resident investor perspective

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This article outlines the main tax aspects when investing in the UK real estate sector, privileging a non-resident investor point of view. Once having set forth some basic preliminary aspects of property taxation, assuming mainly the point of view of an investor (and not of a trader), the article deals with the main tax aspects of letting and disposing properties for individuals and corporate bodies. For individuals, the article explains some available reliefs and special regimes applicable to non-resident investors when letting and disposing properties (for instance, NRL scheme and NRCGT, including for the last one the extension of taxation to the transfer of "property rich" companies shares). For companies, once having dealt with general rules on letting, the article focuses on, inter alia, allowable expenses, the effects of switching for non-resident corporate investors for Income to Corporation Tax provisions and new restrictions using corporate and offshore vehicles. Transfer and Inheritance taxes have been also object of analysis from mainly a non-resident point of view. Eventually, the article provides some synthetic tax planning considerations, highlighting the increasing difficulties in the scenario modified by new rules.

I. General aspects of property investment

Property investment transactions include letting and disposing property, with the aim to holding property for the medium to long period as to obtain a rental income and or capital appreciation. Generally speaking, UK property business consists of any business activities carried on for generating income from land in the UK and any related transactions: taxpayers subject to Income Tax (IT) are taxed under ITTOIA 2005 Part 3, while taxpayers charged to Corporation Tax (CT) are taxed under CTA 2009, s. 205.

Property income consists also of overseas income, which is subject as well to ITTOIA 2005. However, in case of disposal, the relating gain is not to be included in property business but instead deemed as capital gain and therefore subject to Capital Gain Tax (CGT) (CGTA 1995). Indeed, holding properties for a shorter period of time with the view to realising a profit on the sale may have such income to be taxed as a trade instead of as property business[1]: in such a last case ITTOIA 2005 Part 2 is applicable, deriving that such trade is again subject to Income Tax but there are some relevant difference in computation rules.

We need to outline that trade is not a legally predetermined concept but instead is a question of facts, most of them deriving from a vast number of law cases[2].

This article focuses on holding property as investment, therefore privileging a perspective from an investor (and not from a trader), as even if rental business profits are basically

[1] Sarah Ghaffari, ICAEW Tax Faculty, Tax Guide 01/17: let property and Kitty Wanson/Simone Rose, Property investments: some recent developments, Tax Journal, 24 June 2021.

[2] Buying and selling properties within short periods, buying and renovating, selling, managing properties owned by others, collecting rents, providing services connected with properties, providing accommodation services can be considered trading activities. For more details, see please Andrew Crossman, Property tax planning, 2020, Chapter 10, Letting as a trade.

computed using the same principles and rules of a trade (being the taxpayer not considered as trading)**[3]**.

It is eventually worth outlining that in this article no reference is made to the UK legal concept of "*freehold*" or "*leasehold*" rights: generally speaking, even if there can be some differences when dealing with a pure freehold or a leasehold, property income or capital gain deriving directly or indirectly from a freehold or a leasehold share the same general tax treatment (with some exemption, as said before, mainly for computation purposes)**[4]**.

II. Individuals

Individuals with a property investment income are subject to Income Tax at marginal rates (while annual profits are not subject to national insurance). Partnerships and trustees are assimilated for tax purposes to individuals, while a non-resident individual and corporate bodies are to be taxed under Corporation Tax rules as a consequence of the new rules introduced as from 2020.

A. Letting property

Property income is calculated as rents less expenses relevant for tax purposes. Allowable tax expenses are those which are wholly and exclusively borne for the purpose of renting out the property. The range of such expenses include, for example: legal fees for drawing up the tenancy agreements, accountancy fees, advertising for tenants, service charges for leased property, replacement of domestic items, building and contents insurance and cleaning.

The cash basis is the default way to reporting and taxing property business, except for a few exemptions (for example, if the landlord has elected to use the accruals basis or when the business is operated by a partnership).

The first area to be investigated is the tax treatment of finance costs. The UK has always had a very favorable tax treatment of real estate financing costs but as from 2017 has tapered down the tax deduction gradually to tax year 2020/2021, when all finance costs are not deductible. In place of a tax deduction of costs, taxpayers can now benefit from a tax reduction equal to the basic rate value (currently 20%) of the lower of (*a*) finance costs, (*b*) property business profits (net of brought forward losses) and (*c*) adjusted total income (the income exceeding your personal allowance)**[5]**.

Another area of great complexity is represented of tax treatment of costs of capital nature. As a general rule, cost of a repair is an allowable revenue expense and therefore fully deductible from property business income. It is often difficult to distinguish clearly between a repair (allowable as a cost) and an improvement (increasing the capital value of an asset). The key consideration relies on the nature of the work, instead of the quantum of the incurred costs: a repair consists of a restoration of an asset by replacing subsidiary parts of the whole asset, in order to restoring the original function.

It is largely a question of fact and degree in each case whether expenditure on a property leads to an improvement. If the incurred cost significantly improves the asset beyond its original condition, that would be probably a capital expenditure and therefore not a revenue expense deductible in computing property business profits**[6]**.

It is possible to deduct the cost of replacing (not initial purchase) loose domestic items used to furnish a residential property**[7]**, to the extent of course that the capital expenditure rule above described is fulfilled.

Instead of calculating their profits using the normal rules (and thus completing a Self-Assessment tax return), a taxpayer may use a (fixed) property allowance (GBP 1'000 per year).

B. Disposing property and capital gain taxation

CGT is chargeable on gains accruing on the disposal of assets which are not taxable as income, for example in case of a profit from a property dealing trade (TCGA 1992, s. 15, 37). A basic rate taxpayer is taxable at 18% on residential property gains; for individuals other than basic rate taxpayers and trusts the tax is charged at a flat rate of 28%.

Most of the general CGT provisions apply to disposals and acquisitions of land and properties in the same way as they apply to disposals and acquisitions of other assets, save for a number of special rules.

A disposal comprises of all transactions whereby the property ownership is transferred to a third party in exchange of a consideration in cash or in kind. When properties are transferred to connected parties without a consideration, the transfer is considered for CGT purposes as a sale at market value.

Since April 2020 any UK resident disposing of UK residential property deriving thereof a capital gain relevant to CGT shall report and pay such tax within 30 days of completion**[8]**.

For UK resident, CGT report is compulsory only if there is a relevant gain to be taxed. As to calculate the taxable gain, there are a number of costs of capital nature that may reduce the taxable

[3] While rental income is computed using the same rules of a trade, a taxpayer itself is not considered to be trading: the main practical consequence is that this taxpayer may benefit from capital gain tax provisions, while a taxpayer being trading is not allowed to.

[4] In this regard, one of the examples is taxation of a premium. A premium is a lump sum payment made on the creation of an interest in a property. If a landlord receives a premium in relation to a lease of more than 50 years, such premium is a capital receipt, while if the lease has less than 50 years to run, the proceeds are partially capital and property income.

[5] Usually the lower parameter is the total finance costs.

[6] For more details please see HMRC, Property Income Manual, PIM2020 and PIM2030 onwards and HMRC, Business Income Manual, BIM46900.

[7] HMRC, Property Income Manual, PIM3210 expresses in this way "*if the new item is of broadly the same quality/standard as the old item and doesn't represent an improvement then the deduction is the cost of the new item. Note that for these purposes, just because an item is brand new does not make it an improvement over an item which has been in use for several years and suffered general wear and tear*".

[8] For more information, please see ATT, UK Property Reporting Services – a user's guide, September 2021.

amount of gain: professional fees (when buying and selling), land transactions taxes, improvements of capital nature.

C. Private residence and other reliefs

Gains accruing to an individual may be partly or wholly exempt where they arise on the disposal of a dwelling-house or of an interest in a dwelling-house which has been the individual's only or main residence during his period of ownership (TCGA 1992, s. 222[1][a]).

There is no legislative definition of "*interest in a dwelling-house*". On this subject, one may consider an interest in a dwelling-house any type of legal or equitable interest, including all possible forms of ownership**[9]**.

Private residence relief has been object in the last years of a vast number of court cases over some of the requirements. Since an individual may have only one or main residence, it is theoretically possible to have the only or main residence in a home in which they have no interest. This can create conflict where the same person holds more than one property or when he resides in another dwelling-house in which they have an interest. Where there is more than one residence, the individual is able to nominate, within set time limits, which is to be treated as the main residence.

Income from letting furnished residential accommodation normally falls to be taxed as property income (or as trading income, in determined cases). The "*rent-a-room*" relief is however available: rent-a-room receipts up to GBP 7'500 per year are exempt from taxation.

D. Overseas landlords and non-resident investors

If a property is located in the UK, any income generated from it is charged to tax in the UK. Income or Corporation Tax remains chargeable on UK rental income even where the landlord is non-resident**[10]**.

The non-resident taxpayer with rental income has two options of reporting and taxing its income: declaring in a tax return the gross income or using the so called Non-Resident Landlord scheme (NRL). NRL – that it is important to outline is the "*main*" reporting and taxation mechanism**[11]** – is a scheme according to which basic rate Income Tax (20%) must be deducted by the landlord's representative (letting agent, or certain tenants if there is no letting agent), from the UK rental income should the landlords/taxpayer live outside the UK. The letting agent or tenant must pay the tax deducted directly to HMRC every quarter. Special attention shall be given to those subjects that are potentially subject to this scheme: individuals, companies and trustees can be NRLs but shall have the usual place of abode outside the UK.

It is out of the scope of the present article to determine the meaning of place of adobe in the UK, that, not having a statutory definition, is quite complex. Without any claim of being exhaustive, it is possible to say that the concept of tax residence is quite similar to that one of place of adobe but in certain circumstances there can be some differences.

As regards the case of non-resident corporate landlords, companies incorporated abroad and whose main office or other place of business is outside the UK, are considered to have a usual place of abode outside the UK.

An important area affecting non-resident investment is capital gain taxation when they dispose of a UK property. As from April 2019, any direct and indirect disposal by non-UK residents of any UK real estate (irrespective of the use) is subject to non-resident capital gain tax (NRCGT) (CGT, Section 1A and subsequent).

NRCGT is applicable to any chargeable gains realized by non-residents (either individuals or companies) deriving from a direct or indirect disposal of a UK property. The computation rules and tax rates are the general ones for CGT purposes: (*a*) for "*non higher taxpayer*" individuals 18%, (*b*) for "*higher taxpayer*" 28% and (*c*) in all other cases 20%.

NRCGT is applicable also to certain indirect disposal of interests in UK property. The indirect disposal rules apply where a person makes a disposal of an entity, in which it has at least a 25% interest (substantial indirect interest), where such entity derives 75% or more of its gross asset value from UK land ("*UK property rich company*"). Being that a substantive change in UK tax landscape, some investors are still grappling with the implications and therefore new international investors need to carefully verify such rules.

For NRCGT purposes, a "*substantial indirect interest in UK land*" is an interest equal to 25% in the equity and or any other form of participating rights in a corporate vehicle should any time before two years prior the disposal the taxpayer own such percentage**[12]**. Special attention should be given to certain circumstances – for example corporate restructuring or equity transactions – where a 25% interest may not qualify or vice versa: in such last cases, it is appropriate to evaluate all circumstances, while for example considering "*insignificant*" percentage or where it is clear that there were no intention to reach the qualifying 25% interest**[13]**.

[9] For more information, please see HMRC, Capital Gain Manual, CG64470 and ICAEW TAXguide 10/2021: A guide to principal private residence relief. An individual can reside in a dwelling-house in which he or she has no legal or equitable interest is where the property is occupied under licence (a licence is a permission to reside in a property which may be contractual or gratuitous, for instance in the last case, in case of lodgings or staying with family or friends).

[10] There are no double taxation conventions signed by UK which transfer the right to tax to any foreign authority. If the rental income is again charged to tax in a person's Country of residence, then that Country may generally allow a double taxation relief.

[11] In other words, should the taxpayer decide to opt for the self-assessment option, he shall make a claim to HMRC. HMRC shall approve in advance that non-resident landlords receives gross rental income (and subject it to taxation by self-assessment). In all other cases NRL is compulsory.

[12] For NRCGT, when calculating the 25% interest test, chain controlled and connected parties interests shall be considered (for the meaning of connected person please refer to CGTA92, Section 286).

[13] Insignificant is an interest less than 10% according to HMRC approach.

A "*UK property rich company*" is a corporate vehicle of which 75% of its gross (market) value derives from UK land**[14]**.

For NRCGT purposes, key tax issues include the following:

- a charge to NRCGT may arise at more than one level of a corporate structure: in this regard, there are some rules reducing the risk of double taxation – for example in case of investments made by collective funds – but in all other cases only an appropriate tax planning may avoid not desirable results;
- "*the trading exemption*": a disposal is exempted from NRCGT where all, or almost all, of the UK land of the disposed company is being used in the course of a qualifying trade**[15]**;
- attention shall be paid to aggregated disposal of more than one single company and or of members of a group;
- other exemptions regard the substantial shareholding exemption (where however, even with some subtle differences, bearing in mind the concept of qualifying trade, a rich property company disposal would rarely benefit from the substantial shareholding exemption).

There is also a material exemption in terms of NRCGT regarding investments made by collective investment vehicles.

When designing a property investment structure for a non-resident and as to define the scope of application of NRCGT, it is necessary to consider whether the disposer is resident in a country with a double tax convention signed with the UK.

Double tax convention following OECD model assigns the taxation rights in case of capital gain deriving from the disposal of properties or a company whose value is for more than 50% represented by properties, to the Country where the properties are located. It is noteworthy to outline that the OECD model provides a qualifying level of 50% while for NRCGT the level is instead 75% and the relevant interest shall be at least equal to 25%.

Before the amendment to NRCGT in 2019, it was not so uncommon to tackle international corporate structure allowing a total exemption for UK properties capital gains.

The vast majority of UK double tax conventions follow the OECD model even if there are some cases (the most important is the double tax convention with Luxembourg – until such time the relevant provisions are re-negotiated) where the taxing rights are assigned exclusively to the Country of residence of the disposer.

III. Businesses and companies

A. Letting property

The property business profits are calculated on the accrual basis. Therefore, a property business profit (or loss) shall be determined on the basis of general accepted accounting principles, adjusted to take into consideration specific tax rules. In this regard, most of trading IT rules are usually also applicable (even if, as outlined before, a property business is not technically a trade).

A UK property letting business consists of any type of real estate income generating from UK land. There is no difference between locations, type of occupants or category of property: all property income forms part of one and same business. As a consequence, profits and loss across the properties are pooled together. Instead, when a property activity may be considered a trade, each identified trade generates a distinguished pool.

In the UK legislation, rent free property does not count any notional income.

As above already indicated, a property investment company does not carry on a trade from a purely tax perspective: therefore it does not calculate profits but it aggregates from all sources all taxable income against management expenses and changes on income and debit on loan relationships**[16]**. It is however quite important to note that the two approaches, being dissimilar from a legal point of view, are indeed quite similar as results: for computation purposes, it is very common to use the accrual basis mechanism for calculating the profits as if an investment company was trading**[17]**.

In this regard, the main difference arises when dealing with carrying back and forward tax losses and when there is a change in the business (see *infra*).

B. Allowable expenses and losses

A property investment company is entitled to deduct management expenses. There is no a clear legislative definition of management expenses and a distinction between management and property expenses is quite difficult. After a number of cases**[18]**, the rewrite of legislation (CTA 2009, s. 1219[2][b]) has confirmed that management expenses are deductible should an investment be itself held for not an unallowable purpose, with a significant distinction as from trading expenses, for which as being deductible they shall also met the "*wholly and exclusively*" test. Indeed, management expenses are to be considered in most of the cases tax deductible, save for they are of a capital nature. One shall consider that HMRC tends to have a more restrictive approach, amplifying the scope of expenditure of capital nature**[19]**.

[14] It is not usually requested to have formal valuation but instead other market value parameters may be used (valuation for banking or insurance purposes or in absence of other criteria, balance sheet values).

[15] There are a couple of circumstances where a UK land is used in a qualifying trade: when the property is used for carrying out a non-property business or for a UK property development. Letting business is usually not to be considered a qualifying business.

[16] For more information please refer to Robert Maas, Property taxes, 2021/2022.

[17] Indeed, an investment property company is required – first than to file a tax return – to prepare its financial statements according to GAAP.

[18] See, *inter alia*, Camas plc vs. Atkinson, 2004, where it is said, inter alia, that "*the process of reaching a decision to purchase was management in the ordinary sense*".

[19] HMRC, Guidance note, 15 June 2004.

In addition to that, an investment company is expected to make some income: a company with no income might be considered neither a trading neither an investment company. For a property investment company, this condition is very likely to be met: income test may be fulfilled any time in the life of a company.

An important factor is the tax treatment granted to finance costs. From April 2017, finance costs deductibility has been restricted for IT purposes. However, for CT purposes, finance costs may be fully relieved against any corporate profits subject to a tax rules set limiting the interests' deductibility**[20]**.

An interesting and common case is deductibility of remuneration paid to directors. HMRC tends to assume a restrictive approach, distinguishing what is the remuneration for managing the company and what is for managing the properties: in the first case, directors fees cannot be considered as management expenses while in the second case, they may be assimilated to third party expenses (like those of a real estate agent) should they be set on a fair market value**[21]**. Having said that, there is no provision stating a predetermined percentage or amount to directors' remuneration relevant for tax purposes therefore causing that each single case shall be analysed separately.

Eventually, when a property business is making in commercial terms a loss, such a loss is generally also tax relevant against general income in the same accounting period.

Such loss – technically a surplus of management expenses – may be carried forward indefinitely (but not carried back). Unrelieved surplus management expenses appear to be lost also when a company is not longer carrying out an investment business or when it becomes a trading company, while other charges and or capital allowances not relieved in the accounting period they relate to, may be added to the surplus management expenses (CTA 2009, s. 1221 and subsequent).

Attention shall be paid to an investment property company acting not on a commercial basis: in such a case, accrued losses are to be excluded from the property business loss relief (CTA 2009, s. 64 and 67).

C. ATED

Annual Tax on Enveloped Dwelling (ATED) is an annual tax introduced to tackle against using corporate vehicle to hold residential luxury properties. In effect, ATED in its first year (2013) was applicable to properties valued at more than GBP 2 million.

Actually, ATED is payable mainly by companies, partnerships (if they have at least one corporate partner) and collective investment scheme, that own UK residential property valued more than GBP 500'000**[22]**.

The amount of ATED to pay is worked out using a banding system based on the value of your property**[23]**.

There are a number of reliefs and exemptions whereby ATED may be reduced to nil. There are three main reliefs whereby ATED is not applicable: if the property is (*a*) let to a third party on a commercial basis and is not, at any time, occupied (or available for occupation) by anyone connected with the owner, (*b*) being developed for resale by a property developer and or (*c*) owned by a property trader as the stock of the business for the sole purpose of resale.

A connected party is defined also as "*non qualifying individual*": a "*connected*" person is not only a spouse, civil partner and any relatives but also somebody who has an interest in the property (for example, settlor and trustees, partner in a partnership etc.). The fact that the property is rented out even at commercial basis to a "*non qualifying individual*" does not affect the rule highlighted above (and therefore no relief is allowable). Connection for these purposes is determined by reference to CTA 2010, s. 1122, introducing a quite wide test applicable to a very large number of situations. In other terms, even if the property is rented out to connected parties at fair market value conditions, ATED is still applicable.

ATED presents a number of critical aspects whose analysis is out of the scope of the present article**[24]**. In addition to that, ATED-related properties trigger a peculiar and disadvantageous treatment in terms of stamp duty and capital gains taxes (for details see *infra*).

D. Disposing property and capital gain taxation

Chargeable gains are calculated separately from other income of a company, not being relevant if the disposer is an investment company, but added to the income to arrive at the total taxable profits. This computation rule – materially relevant in the past – is nowadays without any significant impact, save for the indexation of expenditure rules.

Most of capital gain tax rules relevant for individuals may be applicable as well as for CT purposes**[25]**.

[20] For more information please revert in this review to Gabriele Schiavone, Tax aspects of UK debt financing, NF 7/2020.

[21] HMRC general approach is that management expenses in a property letting company may be set in a range between 7,5% and 15% of the gross rent. This approach seems not in line with the law provisions and with guidelines which can be extrapolated from *Camas vs Atkinson*. It shall be always borne in mind that an unreasonable remuneration might result in a complete loss of the relief.

[22] For more information please revert to HMRC, Annual Tax on Enveloped Dwellings – Technical Guidance, March 2018.

[23] For properties whose value is up to GBP 1 million, GBP 3'700 tax is due, while when the value is more than GBP 20 million, ATED is equal to GBP 237'400.

[24] For example, when the property is partially rented out and when it is empty for objective external factors.

[25] An interesting point of view, in particular considering the transition rules from income tax to corporate tax, may be found in Claire Lillie, The changing landscape for non-resident corporate landlords, Tax Journal, 26 March 2021.

E. Corporate non-resident investors

Most of the provisions applicable to individual non-resident investors may be valid as well as to corporate non-resident investors (including, for instance, NRCGT and NRL scheme).

While in the past it was quite widespread using entities incorporated in an *offshore* jurisdiction for investing in the UK real estate sector, since at some conditions capital gain and commercial rental income could have been exempt, *offshore* companies are actually comparable for tax purposes as to a resident entity.

As noted above, with effect from April 2020, non-resident companies have "*switched*" from Income to Corporation Tax with the effects seen before. In this regard, special attention shall be given to withholding obligations: any external debt secured over an underlying UK real estate is deemed to accrue interest subject to 20% domestic withholding tax**[26]**.

The UK has promoted over the years property investment by "*regulated*" vehicles. An analysis of tax aspects relating to property investment by a "*regulated vehicle*" is outside the scope of the present article**[27]**.

IV. Indirect taxation

A. Taxes on purchase

Stamp duty land tax (SDLT) is applicable to sales and transfers of properties as a percentage of the chargeable consideration (normally the purchase price)**[28]**.

SDLT is a quite complex area of law, rich in jurisprudential cases and HMRC interpretations: in this article we would focus on some main aspects, privileging a non-resident perspective.

The purchaser of residential property has to pay SDLT according to the transfer value: up to GBP 125'000 nil rate, the next GBP 125'000 2%, the next GBP 675'000 5%, the next GBP 575'000 10% and above GBP 1,5 million 12%**[29]**.

Any non-natural purchasers are subject to a 3% supplement as well as for second-home property buyers.

In case of transfer made by non-resident, the transfer of a residential property is subject to an addition surcharge equal to 2% to be added to the 3% supplement above mentioned**[30]**.

For surcharge purposes, a bespoke definition of residence is applicable for individuals (FCA 2003, Schedule 9A): if a taxpayer is not present in the UK for at least 183 days during the 12 months preceding the purchase, the same is deemed non-resident for SDLT purposes (even if still resident for IT). Interestingly, it is possible for an individual to change status from non-resident at the date of effective purchase by the end of tax period (in these cases, HMRC has provided a special relief for repayment).

Should the acquisition be made by a non-resident company, the legislation above mentioned has introduced as well as a peculiar concept of residence for SDLT purposes. Schedule 9A above says that a chargeable transfer is subject to the surcharge if following conditions are met: (*a*) the company is not resident in the UK for CT purposes or (*b*) the company meets the conditions set forth in Schedule 9A 7(3) (a close non-UK controlled company).

A company may be considered as a close company if it is within the definition given in Chapter 2, Part 10 CTA 2010. A company is deemed to be closed for CT purposes if it is under the control of 5 or fewer participators or participators who are also directors. A participator may be defined as a holder of shares or of other equivalent voting and or economic rights.

For the surcharge purposes a company meets the non-UK control test if their relevant participators are non-resident for SDLT purposes**[31]**. Hence, it is sufficient to follow the definitions of close company for CT purposes with some modifications. It appears therefore that a company whose management and control is exercised in the UK – having for instance all board of directors members resident in the UK – if participated by non-resident shareholders (individual or corporate), can be considered a close non-UK controlled company for SDLT purposes.

The application of the surcharge on acquisitions by some non-natural person (*i.e.* trusts) looks set to become very complicated and is not considered in detail in this article.

B. Inheritance aspects

The standard rate for Inheritance Tax (IHT) in the UK is 40%, thus representing a key tax element when investing in the UK real estate sector.

Inheritance tax is a very complex area of taxation: in the lines below, I provide some basic information, privileging a non-resident perspective.

[26] See again, for more details on the UK withholding tax regime, in this review Schiavone (note 20).

[27] For more information please also see, inter alia, Robert Maas, Property Taxes 2021/2022, Real estate investment trusts, Alex Tostevin/Andrew Cromb, The real estate investments structure taxation review, July 2021 and HMRC, Investment Funds Manual, 2022; for an Italian perspective, please refer to Alberto Franco, Tassazione delle plusvalenze immobiliari in Regno Unito: novita' per i soggetti non residenti, Il Fisco nr. 21, May 2019.

[28] SDLT is a transfer tax applicable to transfer of properties located in England, while in Scotland and Wales such a tax is differently named (respectively LBTT and LTT). For the purposes of this article, we refer for sake of simplicity to SDLT, even if there can be some material differences (for example in rates) between the aforementioned transfer taxes.

[29] There are special rules available to first-home buyers (no SDLT up to GBP 300'000, 5% on the portion from GBP 300'000 to 500'000), but only if the total value is not over GBP 500'000.

[30] For a comprehensive analysis see HMRC, SDLT Manual, 09850 and subsequent.

[31] Please refer to HMRC, SDLT Manual, 09920.

A property located outside the UK is deemed excluded property for IHT purposes (ITHA 1984, s. 6) if the individual beneficially entitled is domiciled outside the UK. As a consequence, if you are not domiciled in the UK (irrespective of being resident), the chargeable transfers relevant for IHT purposes would include only assets located in the UK.

The notion of domicile for IHT purposes differs in some aspects from domicile for Income Tax purposes: HMRC may treat an individual as being domiciled if he lived in the UK as resident for 15 of the last 20 years (and he was also resident for at least one of the four tax years or if we was domiciled in the UK within the last three years). As a consequence, it would be possible that an individual, having ceased to be resident for Income Tax purposes, can be still considered deemed domiciled in the UK for Inheritance Tax purposes.

An interest in a close company (or partnership) whose value is directly or indirectly attributable to a UK residential property is within the scope of IHT (ITHA 1984, Sch. A1)**[32]**. Therefore, a non-domiciled individual holding shares in a non-resident company which at its turn has an interest in a UK real estate and or an interest in a company or partnership owning a UK real estate, is potentially subject to IHT.

There is a *de minimis* rule exemption, where the value of a relevant interest in a close company is less that 5% of the total value of all the interests. In such a case, such value is disregarded for IHT purposes: it shall be borne in mind that the *de minimis* exception applies by reference to the shareholdings to the value of UK residential property (and not by reference to the percentage of UK assets over non-UK assets).

The same rule is applicable to loans used – directly or indirectly – to finance an acquisition of UK property.

An interesting case is when a UK property is held directly or indirectly by a trustee. Indeed, as a general rule, a settled property situated outside the UK is excluded property if the settlor was domiciled outside the UK at the time the property was comprised in the settlement (IHTA 1984, s. 48[3][a]). As a consequence, shares in a non-resident company held in trust are to be considered excluded property, save for rules Sch. A1 as above are applicable, but should the property investment be in a non-residential or mixed use properties, the shares would be again excluded property. In this regard, according to HMRC approach (Statement of Practice SP E9, 2012), where a property is added to a settlement, it is relevant the domicile of the settlor at the time when such addition has been finalized.

C. VAT

Residential letting is exempt from VAT, save for specific cases (for instance, standard rate applies for serviced and or holiday accommodation, should the landlord be a VAT subject exceeding taxable threshold).

[32] For more details please refer to ICAEW, TAXguide 08/19, May 2019. One shall bear in mind that such rules apply only to residential properties.

Commercial properties transactions are usually subject to standard-rated (20%). However, lease of a commercial property or old commercial building (older than 3 years) are not taxable unless option to tax election is made.

Whenever there is an exempt supply of commercial land or buildings, the owner has the option of changing it to standard-rated supply by "*option to tax*" election.

V. Tax planning considerations

Over the last few years, the UK tax landscape for overseas investors in the UK real estate has seen dramatic changes. Most of them have been highlighted in the chapter above and generally speaking, it is possible to say that new UK rules on property transactions have increased the overall tax burden. As a consequence, it is more and more important to consider any possible tax planning opportunities and to take any steps in order to mitigate the investor global tax burden and optimize its ROE.

This implies to take necessary steps at the outset of a transaction to understand nature of the proposed investment, identity, circumstances and tax status of would-be investors as to ascertain the most efficient corporate structure.

From a UK tax point of view, it is possible to figure out a number of "*investment cases*" with different solutions.

Should the investment be in commercial properties, individuals and corporate investors have different options. Assuming that an investment is made by a resident vehicle (a company or a partnership) – a very probable circumstance for a number of corporate and tax factors (including for instance VAT) – individuals may consider the use of a holding company. For non-resident and non-domiciled investors, such holding may usefully be incorporated in a foreign jurisdiction. It is also possible to invest directly by a non-UK company: in any case, the latter shall be subject to the same CT rules applicable to resident companies.

Even for resident not domiciled, there is room for a proper tax planning, for instance using a foreign trust structure.

A partnership may be a valuable solution, in particular if the investor is resident in a country where partnership income is not deemed a financial income (as a dividend) and potentially entitled to a tax credit relief: indeed, while the property income is calculated and taxed in the UK, the net proceeds received by the same investor may be relieved from a double taxation exempting them from domestic income tax or benefitting from a tax credit relief.

For individuals, one shall bear in mind that using a non-resident company, the shares of the latter are considered "*excluded property*" for Inheritance Tax purposes.

Should the investment however be in residential properties, ownership corporate structures have been under the hammer and object, as seen before, of punitive tax measures.

In case of a residential property used for personal purposes, it is highly recommended – from a tax perspective – to invest directly as individual: using a corporate structure, this would not bring any tax advantages (for example in terms of stamp duty when acquiring) while actually triggering various tax inefficiencies (for example ATED and an higher capital gain tax rate).

In case of a residential property business for investors, rental income and capital gain are taxed at Corporation Tax rates but can benefit from a set of provisions allowing a vast number of costs to be deductible, including, *inter alia*, an overall favourable finance expenses tax regime. In this regard, international finance strategies may be properly designed as to maximizing tax deduction and optimizing withholding tax obligations.

One shall always bear in mind that residential properties investment would trigger an Inheritance Tax matter: especially if the investment is made by a so called "*family company*", one possible solution is to use a foreign trust. For non-resident and non-domiciliary individual, such strategy shall be carefully designed according to country of residence tax rules affecting settlor and beneficiaries.

Let's we introduce an example: a non-resident and non-domiciled settlor sets up a international discretionary trust, whose beneficiaries are his/her heirs (not vested). It is possible to figure out a couple of scenarios: the settlor dies before seven years as from the trust has been set up (and the property assigned to), or after. While in the last scenario it seems coherent to consider the *mortis causa* event not triggering an IHT chargeable transfer since *inter alia*, after the qualified period of seven years**[33]** the transfer become definitively exempt, in the first, one shall investigate if there would be a chargeable transfer assuming the trust elements and qualified individuals have not changed during such a period (for instance no beneficiaries are been vested).

[33] One shall bear in mind that, after a qualified period of time (7 years), gift and no consideration transfers are to be considered "*consolidated*" for IHT purposes and therefore become definitively exempt.