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Insights

NEW RESIDENTIAL PROPERTY DEVELOPER TAX: THE DESIGN OF THE TAX

Oct 04, 2021

SUMMARY

In this blog we consider the current design of the residential property developer tax (RPDT). Separately we have blogged on the triggers for liability. This blog is based on the current draft of the legislation issued on 20 September. The final design of the tax has not been decided, and will be announced in the Budget on 27 October (together with the rate). A key outstanding element is whether the tax extends to the build to rent (BTR) sector, which is currently being considered by HM Treasury.

WHO IS LIABLE?

The person liable to pay RPDT is a corporate residential property developer that undertakes residential property development activities in relation to UK land. The developer needs to be within the charge to UK corporation tax for RPDT to apply.

As explained in our blog on the triggers for liability (here) the definition of residential property development activities is broad and includes seeking planning permission, marketing as well as dealing in property or constructing it. Significantly, the developer or a "related party" has to have or had an interest in the land, so RPDT does not apply to third party developers. This may lead to a disparity in treatment between owners who develop themselves and those that use third party contractors. Also, the land interest has to be part of trading stock (which is a term defined in the draft legislation).

HOW IS THE TAX DESIGNED CURRENTLY?

The tax applies to profits from *residential* property development arising on or after 1 April 2022. So in a mixed property use scenario, it applies just to profits from the residential part.

The tax applies to the trading profit for corporation tax purposes, as adjusted (the "adjusted trading profits") and after applying the RPD loss rules. Starting with the corporation tax figure to arrive at

RPD profit should provide some simplicity. The adjustments strip out these features amongst others: profits from non-residential activities, any interest expense (so tax deductible interest is added back) and any corporation tax losses and capital allowances. Notably, HMRC did not agree with the many requests to exclude interest expense from adjustment, so this is bad news for highly leveraged deals.

Elsewhere there is some complexity (but fairness) with the RPD loss rules proposed. There are a series of rules allowing for the use against RPD profits of carried forward RPD losses and the surrender of RPD losses through group relief (whether current year RPD losses or carried forward ones). There are many similarities with the rules for corporation tax losses, including a rule restricting the use of carried forward RPD losses against only 50% of RPD profits.

The tax is charged on any RPD profits exceeding an annual allowance. The allowance is there to ensure that only large residential property developers are taxed. Although £25m was mentioned in the consultation document, the draft legislation does not state the allowance. We expect the amount to be announced at the Budget alongside the rate. There are rules allocating an allowance around group members and a default provision applies when no group member has been nominated to allocate. (Unusually, there are provisions dealing with the allocation of allowances between joint venture members and joint venture companies, which we touch on below).

HOW ARE JOINT VENTURES BEING DEALT WITH?

In the consultation document there was an ambiguous reference to joint ventures. HMRC is now much clearer in its proposals for joint ventures.

In the draft legislation joint ventures are impacted in three ways.

Firstly, a joint venture company is treated as “related” to a joint venture developer that has at least a 10% equity interest in the company. This means that the RPDT can apply where a joint venture company holds an interest in the land while a joint venture member develops it. This extends the definition of related party beyond a group.

Secondly, a joint venture company’s RPD profits are allocated to (and subject to RPDT in) a developer with at least a 10% equity interest in it if the joint venture company is closely held and does not pay RPDT because its profits fall below its allowance.

Thirdly, there are provisions for the operation of the allowance where a member of a joint venture company is exempt from corporation tax.

ANTI-AVOIDANCE RULES

There are anti-forestalling rules that apply where a person is trying to avoid the RPDT by accelerating profits so that they fall within an accounting period ending before 1 April 2022. The rules try to stop such arrangements working.

ADMINISTRATION OF THE TAX

The RPDT is treated as if it was an amount of corporation tax. It is chargeable in respect of a chargeable accounting period for corporation tax purposes. A range of administrative provisions that apply to corporation tax equally apply to RPDT. A person making a payment of RPDT must notify HMRC of the payment so that HMRC can track the tax.

COMMENT

HMRC has listened to a number of comments made in the consultation, e.g.

- using the trading profit for corporation tax purposes as a starting point to calculate RPDT, and
- excluding student accommodation (which requires expected occupation of at least 165 days a year) and care homes of different types.

Elsewhere the rules on RPD losses are complex, but provide fairness where profits fluctuate year on year and are at least familiar.

Big points outstanding are the tax rate, the allowance and whether it will apply to BTR.

For further reading see our blog on the triggers for liability in the draft legislation and our blog posted after the consultation was issued in April.

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MEET THE TEAM

Elizabeth Bradley

London

elizabeth.bradley@bclplaw.com
+44 (0) 20 3400 2323

Anne Powell

London

anne.powell@bclplaw.com
+44 (0) 20 3400 2162

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