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Insights

IMPACT OF UK AUTUMN BUDGET ON REAL ESTATE SECTOR

Oct 27, 2021

SUMMARY

It was a relatively light Budget for the real estate sector. Highlights included the long-awaited announcement of the rate of the residential property developer tax and some reform of business rates. There were also announcements in the real estate fund space.

Residential property developer tax

The key development was the announcement of the rate of this tax at 4%. Rumours had been circulating that the rate would be set between 3-5%, so the rate is as expected.

In the responses to the consultation published today, the government says it remains of the view that the tax should be time-limited and that it should raise at least £2bn over a decade. However, it does not want to commit to repealing the tax at the ten-year point up front and says that it will repeal it “once sufficient revenue has been raised”.

The government has had to pitch the rate at a level that it believes will not deter residential developments. No doubt, it will keep this rate under review during the ten-year period the tax is intended to run. Will the Chancellor (or future Chancellors) increase the rate if it looks likely that the aimed for £2bn is unlikely to be met over that period, or if costs of cladding remediation work increase? Or will the tax just be charged for longer at the 4% rate?

The government confirmed that the annual allowance will be set at £25m (again, as expected) so that it targets the tax at large corporate residential property developers.   If a developer has residential property developer profits below £25m, it will not pay the tax.

As trailed previously, build to rent will not be within scope. In the response document the government says the exclusion has been made at this point in time and will be kept under review.

More guidance is given on the exclusion for the retirement living sector. The government wants to focus this exclusion on just care homes and is not minded to include “extra care housing” or “housing with support” in the exclusion. The government treats the latter two as more akin to mainstream residential dwellings that just happen to be marketed to older people.

Again, the government confirmed the exclusion for student accommodation (which requires expected occupation of at least 165 days a year).

In a situation where a landowner has sold a property with an overage, the government clarified that it does not expect the original seller with an overage to be subject to the tax.

REIT

The government reconfirmed the first phase of REIT changes, which will be introduced from April 2022. These changes were announced in July and were covered in our earlier blog. In brief the changes:

- remove the requirement for listing of the REIT’s shares where 70% of its ordinary shares are owned by institutional investors (including pension schemes, sovereign wealth funds, long-term insurers and UK and non-UK REITs) - the ownership level of 70% is down from the originally proposed 99%, so we expect more detail, and confirmation of this change, in the Finance Bill to be published on 4 November;

- allow a non-UK REIT to qualify as an institutional investor provided it, the entity, meets the test of equivalence with a UK REIT, so it will no longer be necessary for the non-UK REIT regime itself to meet the equivalence test;

- will ensure that a REIT will no longer be taxed where distributions are made to corporate shareholders that have at least a 10% interest in the REIT where the shareholder is entitled to receive the distribution gross, e.g. a UK company; and

- include limited changes to the balance of business test, which requires 75% of a REIT’s assets and income to derive from its property rental business.

The government is considering a further set of REIT changes to improve access to the regime as part of a wider REIT review. The government says it will publish its responses to the review of the wider funds regime “in the coming months”, so hopefully, we will not have long to wait before knowing which of the reforms it plans to take forward.

Other fund developments

The government reconfirmed the introduction of a new regime for qualifying asset holding companies (“QAHCs”) that meet certain tests from April 2022. The government aims to make the UK more competitive as a holding company jurisdiction and to make UK funds more attractive.

However, it has had limited time to put in place a complex new regime to compete with the likes of Luxembourg (amongst others), so it will be interesting to see the detail of the QAHC regime in the Finance Bill due to be published on 4 November.

One question for real estate funds is how this regime can be used alongside a REIT when the QAHC will exempt profits from non-UK real estate from tax, although not profits from UK real estate (which could be exempted in a REIT).

Please see our earlier blog on the QAHC.

The government is considering other measures to support UK global competitiveness. It is consulting on allowing non-UK incorporated companies to re-domicile to the UK. Businesses will be interested that it is thinking about allowing those companies to bring their assets into the UK tax net at their market value at the time of the redomiciliation.

The government reiterated its plans to consult on options to simplify the VAT treatment of fund management fees. This consultation was promised some time ago. It will now be published “in the coming months”.

Business rates reform concluded

The review into the reform of business rates has now concluded after an extended period. Fundamental reform is not on the cards, but some helpful changes will be made. These include relief focussed at the retail, hospitality and leisure sectors. They will benefit from a 50% business rates discount for 12 months up to maximum of £110k. In addition, retailers will also welcome the government continuing to consider an online sales tax. The government has not made a decision yet whether to introduce the tax, but says that if it does, it would be used to reduce business rates for retailers. If this idea is introduced it would go some way to rebalance the tax burden between bricks and mortar shops and online retail. The government will publish a consultation on an online sales tax “shortly”.

The green agenda is referenced in the business rates reform. There will be a business rates exemption from 2023 until 2035 for investment in plant and machinery for green energy improvements to buildings. This announcement is well timed coming only four days before COP 26 in Glasgow. The relief will help support the government’s green agenda and comes as part of a package of measures encouraging green energy and decarbonisation investments in buildings, whether residential or commercial.

No stamp duty land tax changes

For once, there were no announcements on stamp duty on residential properties. There were no holidays, new rates or new charges targeting a particular type of homebuyer.

Extension of time period to pay capital gains tax on sales of UK residential property

The government is giving sellers of UK residential property within the scope of capital gains tax (e.g. second homes) an extra 30 days to pay the tax and submit the tax return. They will now have 60 days rather than 30 days for sales completing on or after 27 October 2021.

Freeports

At Spring Budget 2021, the government announced eight Freeports in eight English regions, to encourage businesses from around the world to create new hubs of global trade. Freeport status is associated with a series of tax breaks. The first tax sites will be in Humber, Teesside and Thames. Those Freeports will be able to begin initial operations from November once legislation to be laid on 29 October has been passed. The government remains committed to establishing at least one Freeport in Scotland, Wales and Northern Ireland.

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