Briefing

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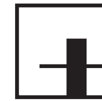

Rural Property Tax Update

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With the advent of a new tax year here is a round-up of the most significant changes to tax on property that landowners need to be aware of.

1. Land and Buildings Transaction Tax (LBTT)

1.1 Additional Dwelling Supplement

On 1 April 2015, SDLT was replaced in Scotland with the new Land and Buildings Transaction Tax (LBTT). From 1 April this year there will be further changes to the transaction tax in Scotland as the 'Additional Dwelling Supplement' will be payable on certain purchases by individuals of second dwellings valued at more than £40,000 and on certain purchases by companies. The 3% additional tax is aimed at levelling the playing field for first time buyers.

However, those already on the property ladder simply looking to move home, could be caught out by the additional charge. The final Bill allows for a grace period of 18 months where the 3% tax can be reclaimed if the sale of the previous main residence concludes after purchasing the new main residence.

If applicable, the additional 3% charge is payable on the whole of the value of the new property being purchased. A buyer purchasing a property for less than £145,000 (generally exempt from LBTT) would have to pay 3% on the whole value of the property if they have not sold their previous main residence before purchasing their new main residence. Of course, if the previous main residence was sold within 18 months of the purchase of the new home, the tax can be reclaimed but must still be budgeted for at the stage of the purchase of the second home.

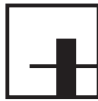
The question asked by many is whether 18 months is a sufficient length of time to reclaim. If the chain breaks down, and a homeowner who has purchased their new house is not able to sell their previous residence before the end of the 18 months period, there will be no opportunity to reclaim the additional tax paid.

A comprehensive analysis of the 3% charge can be found here.

1.2 Lower Rates for Agricultural or Commercial Property

As with SDLT, LBTT applies lower rates to agricultural properties. Farms and agricultural property will be taxed at the non-residential rates, as will purchases of 'mixed' residential and non-residential property. The difference between the residential (ranging between 0% - 12%) and non-residential (0% - 4.5%) rates of tax for LBTT are more prominent than in the SDLT system. As a result large tax savings can be made when purchasing farmhouses if agricultural land is included in the sale. This would make the transaction 'mixed' and as a result the lower non-residential rates would apply.

The current Revenue Scotland LBTT Guidance is fairly sparse and there is little guidance on what constitutes agricultural property or buildings. Looking south to HMRC's guidance in relation to the similar SDLT rules, non-residential property (including agricultural property) is defined by exclusion. That is to say that any property



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that does not fall within the category of being 'residential' will be treated by default as non-residential.

1.3 No equivalent to 15% SDLT Charge

In England and Wales, a 15% tax rate for the acquisition of residential property by companies and properties is levied on the purchase price. When compared with the highest rate of residential SDLT and LBTT tax being 12% for individuals, the 15% charge's purpose appears to be to discourage companies investing in residential property – a topic on which we expand in section 2 below.

Although there is no direct equivalent in Scotland, the new 3% Additional Dwelling Supplement will automatically apply to any residential property acquired by a company. This is the case even where the property is the first residential property held by the company. As a non-natural person, such as a company, cannot have a main residence the purchase of a residential property is deemed to be a purchase subject to the 3% tax charge.

2. Annual Tax on Enveloped Dwellings (ATED)

In addition, companies that simply own residential property need to be aware of the changes to the Annual Tax on Enveloped Dwellings. This less well known tax is intended to discourage the holding of high value residential property (HVRP) through companies, rather than directly by individuals.

The advantage of holding ('enveloping') property in a company and selling shares in the company rather than selling the property directly, is that stamp duty on shares is considerably cheaper than SDLT or LBTT (0.5% on UK shares compared with 12% as the top residential rate for both SDLT and LBTT).

To offset this potential tax saving, an annual charge is levied on properties both north and south of the border meeting certain criteria.

2.1 The HVRP Threshold

When ATED was first introduced, the HVRP threshold was £2 million. This fell to £1 million last year, and as of 1 April 2016, the threshold is just £500,000.

2.2 ATED Checklist

In addition to meeting the HVRP threshold, there are a number of other criteria that must be met before the charge is payable. In particular,

- the HVRP must be owned by a chargeable person (a company, collective investment scheme, or partnership with at least one corporate member); and
- for at least one 'chargeable day' (a day not attracting relief) during the chargeable period of 1 April to 31 March each year.

If these criteria are met, an ATED charge is payable for that year in bands based on the value of the property. The rates from 1 April 2016 are as follows:

Value of Property	Charge
Over £500,000 up to £1 million	£3,500
Over £1 million up to £2 million	£7,000
Over £2 million up to £5 million	£23,350
Over £5 million up to £10 million	£54,450
Over £10 million up to £20 million	£109, 050
Over £20 million	£218,200

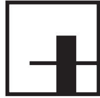
2.3 ATED Reliefs

Clearly the scope of ATED is potentially very wide, particularly as the HVRP threshold continues to be reduced. In order to not affect genuine commercial activities, a number of reliefs are available. Reliefs are applied on a pro-rata basis to the ATED charge based on the number of qualifying 'relievable days'. Four of these reliefs most relevant to Rural Property and Businesses are outlined below:

- Rental Business Relief can be claimed where the property held by the company is being let for commercial purposes. The relief is also available where the property is held as a rental property, but at the current time the owner is taking steps to sell, demolish or convert the building.
- Employee/Partner Occupation Relief is available where an employee or partner (and their family) lives in the property owned by the company. However, this can only apply where the employee/partner is not entitled to 10% or more of the profits of the company and the property is made available solely for the purposes of the trade.
- Farmhouse Relief applies in the case of a (former) farm worker, or their surviving spouse, living in the property owned by the company. In order to be considered a farm worker, the individual must be involved in either the day-to-day work, or the direction and control, or the farming trade. The property itself must not be too detached from the land used for farming in order for the relief to be available.
- Where a property is opened to the public as a source of income commercially, and the public are offered the opportunity to enjoy the property on at least 28 days a year, the Dwellings Open to the Public Relief can be claimed. Interestingly, this opportunity need not be taken up by the public in order for the relief to apply. For example, a wedding venue may be available for hire every weekend of the summer, but only having bookings on 20 days in the year. In this case, the relief can still apply.

2.4 Practical Comment

Although the intention of ATED may be to reduce avoidance of SDLT/LBTT through the use of companies, it has been reported that the result so far has been to raise five times more tax than anticipated, seemingly



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without materially discouraging the holding of residential property through companies. As the threshold for ATED is halved (again) in the coming tax year, more properties will be affected.

The key practical points to bear in mind are that there only needs to be one 'chargeable day' within the period 1 April to 31 March for the tax to be payable. And if there is a chargeable day within the next chargeable period, the ATED will be payable again.

Even where one of the reliefs can be claimed to reduce the charge payable to nil, an ATED tax return will still need to be filed. Only where the property does not meet the criteria set out above, making it exempt from ATED, will the owners not have to complete a return.

For further information or advice on any of the issues discussed in this briefing note, please get in touch with your usual Shepherd and Wedderburn contact.

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