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Non-resident capital gains tax: the new regime

The UK has introduced new rules which radically change the tax landscape for non-residents investing in UK property.

Prior to the introduction of the new rules, a non-resident would have been outside the scope of UK tax on chargeable gains on the disposal of a UK commercial investment property or a disposal of shares or units in a property-owning SPV.

But under the new rules, which apply **from 6 April 2019**, non-residents will now be subject to UK tax on chargeable gains on both:

- *direct disposals* of UK land; and
- *indirect* disposals of UK land.

The new rules apply whether the UK land in question is commercial, residential or mixed use and there is no requirement for the non-resident to have any UK branch, agency or other UK presence. The rules cover disposals by non-resident individuals, companies, trusts and other entities.

A **direct disposal** simply means a disposal of a direct interest in UK land (including disposals through tax transparent partnerships).

An **indirect disposal** is a disposal of shares or units in a company or other relevant entity that is "UK property rich". A company or other entity is **UK property rich** if 75% or more of its gross asset value derives directly or indirectly from interests in UK land. In applying this 75% gross asset value test, value can be traced to UK land interests through any number of entities in a property holding structure.

The new charge on *indirect disposals* means that, for example, non-residents disposing of shares or units in a UK property rich company, JPUT, REIT or property fund (whether the entity is UK-based or overseas) could now be subject to UK tax.

Helpfully, the new rules provide for a **tax rebasing** of interests in UK land and shares or units in UK property rich entities that were held by non-residents on 5 April 2019. The tax base cost of the relevant asset is deemed to be equal to its market value on that date. The effect of this rebasing is that only gains accruing from 6 April 2019 should be brought into the charge to UK tax under the new rules. Where the original tax base cost would have been higher than the 5 April 2019 market value, it is possible to elect to keep the original tax base cost. As a practical matter it will be very important for non-residents to have appropriate **evidence** of the market value of the interests in UK land and UK property rich entities held by them as at 5 April 2019.

In relation to *indirect disposals* (i.e. disposals of shares or units in UK property rich entities) there is a **safe harbour** for non-residents who have held a **less than 25% investment** in the entity in question throughout the two years prior to the disposal. This 25% investment test looks at both economic and voting rights and requires rights and interests of connected persons to be aggregated. Where the safe harbour applies, an indirect disposal by a non-resident is outside the scope of the tax charge under the new rules.

The *<25% investment safe harbour* mentioned above does *not apply* to disposals that relate to a collective investment vehicle. A **collective investment vehicle** for these purposes means an entity that is a "collective investment scheme" or "AIF" for regulatory purposes and also includes UK REITs and certain non-resident companies that have characteristics similar to a UK REIT. This will include most property funds and also JPUTs. Disposals through partnerships can also fall within the regime for collective investment vehicles and therefore may also not benefit from the safe harbour, depending on the circumstances.

The rules contain detailed rules relating to the treatment of collective investment vehicles. These include the ability to make a **transparency election** or an **exemption election**. Broadly, the effect of these elections is to move the point of taxation away from the collective investment vehicle itself (or the wider fund) and up to the investor level. Specific UK tax advice should therefore always be sought in relation to investments in, or transactions involving, collective investment vehicles that are UK property rich.

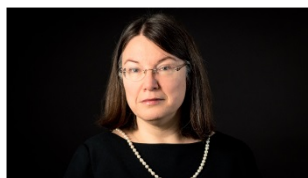
One other change to note is that, from **April 2020**, non-resident companies with **UK property rental income** will be brought within the charge to UK corporation tax on that income, rather than being subject to *income tax* as is currently the case. One benefit of this is that the lower corporation tax rate will apply (it is currently 19% but is scheduled to reduce to 17% from 2020). But it will also mean, for example, that more restrictive computational rules such as the "corporate interest restriction rules" may apply. This could reduce the level of interest expense that can be treated as tax deductible.

In light of these very significant tax changes, non-residents who hold, or are undertaking any transactions involving:

- interests in UK land; or
- entities that directly or indirectly hold interests in UK land

should seek UK tax advice in relation to the tax consequences of the new rules for them, including their UK tax filing and payment obligations.

Get in touch



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